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Budget & Tax News

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THE MONTHLY NEWSPAPER FOR TAX ISSUES

V2 N5 ~ MAY 2004

Medicare Will Be Bankrupt by 2019



U.S. Health and Human Services Secretary Tommy Thompson (left) and Treasury Secretary John Snow say hospital payments for the elderly under Medicare will exceed income for the first time this year, nine years earlier than anticipated. The federal program's assets will dry up in 2019, seven years sooner than expected.

Taxpayer groups sound alarm in wake of Trustees' report

by Tom Schatz

Citizens Against Government Waste (CAGW)—the 20-year-old watchdog group dedicated to eliminating waste, fraud, abuse, and mismanagement in government—on March 25 criticized national leaders for “overseeing the fiscal deterioration of the Medicare program over the last four decades.”

CAGW's criticism came in response to a report issued a day earlier by the trustees who monitor the fiscal health of Medicare and Social Security. The trustees estimate the fund for hospital bills in the Medicare program will run dry by 2019, seven years sooner than predicted last year, largely thanks to the new Medicare bill. Medicare begins dipping into its trust fund for the first time this year.

“Politicians in Washington ignored this problem for several decades, and then they make it worse by adding a costly prescription drug benefit,” CAGW President Tom Schatz said. “The retirement

MEDICARE p. 9

Cal. Taxpayers Rout Prop 56

by John Skorburg

On March 2, California voters soundly rejected Proposition 56—a proposal opponents said would make it easier for state policymakers to spend more and increase taxes to pay for their extravagance.

Sixty-six percent of California voters rejected the measure, thereby keeping in place the state's requirement that no budget and budget-related tax and appropriation bills may pass without a two-thirds majority of the legislature.

CALIFORNIA p. 6

Fla. Reforming Its Privatization Efforts

by Geoffrey F. Segal

On March 11, Florida Governor Jeb Bush signed an executive order directing the state's Department of Management Services to create a “center of excellence” authorized to conduct a statewide evaluation of Florida's outsourcing efforts. The new Center for Efficient Government is also empowered to “identify opportunities for additional outsourcing initiatives, and oversee execution of future outsourcing projects.”

In a report issued in June 2003, the Governor's Inspector General found problems statewide with contracting. The report said agencies “often don't have in writing [exactly] what they're

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Kentucky Unveils Tax Reform Plan

by John Skorburg

Kentucky Governor Ernie Fletcher unveiled a far-reaching “tax modernization plan” during a news conference on March 11 in Frankfort. The plan reduces marginal income tax rates, extends the corporate income tax to new entities, and increases or expands a wide range of excise taxes.

Fletcher, a Republican who took office as governor in December, said he will “ask the state's General Assembly to pass a bipartisan bill that will remove 125,000 low-income individuals from the tax roles while stimulating the state's economy and creating jobs across the state,” according to the news release from his office.

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STATE UPDATE

Poll Shows Ohioans Favor Spending Restraint, Oppose Tax Increases

by Joshua Hall

Ohio citizens believe the state is going in the wrong direction, and economic concerns trump other issues, according to poll results released on February 25 by the Columbus-based Buckeye Institute for Public Policy Solutions. The poll found strong support among registered voters for solving future budget woes by cutting state spending, not raising taxes.

"The economy remains the dominant issue for elected officials in Ohio," observed Sam Staley, president of The Buckeye Institute and principal author of the report. "But Ohioans recognize the state's approach to state spending and tax reform may be linked to future economic progress."

The poll, conducted by the internationally recognized firm The Tarrance Group, found strong support for particular types of tax reforms, including shifting revenues to user fees and moving toward a flat-rate income tax. Among the poll's other findings:

- 86 percent of poll respondents believe lawmakers should focus on spending restraint rather than increasing taxes to address future budget deficits.
- 73 percent understand tax rates influence the decisions of wealthy families and businesses to stay in or leave Ohio.
- 96 percent understand state taxes influence the decisions of businesses to stay in Ohio.
- 78 percent would support a proposal to limit state spending growth to the inflation rate.
- 60 percent would support reforms that simplify Ohio's income tax system by moving toward one rate for all taxpayers.

The poll is noteworthy because it is among the first publicly released surveys aimed at understanding how Ohio citizens feel about particular tax reforms and fiscal policy. "As our elected officials come to grips with Ohio's ever-pressing budget and tax reform issues," Staley said, "the results of this poll will serve as an important benchmark."

"This study examines fiscal policy reform from a political perspective," noted Staley. "The Buckeye Institute has published numerous studies on tax reform, but many of these analyses have relied on academic and statistical analysis.

They have not given significant attention to the political environment in which tax reforms would be implemented. This analysis seeks to fill the gap."

While the recession may have influenced the results, "Ohioans were specific about the nature of the problems faced by the State," the report said. "Ohioans ranked jobs, unemployment, and taxes among their top worries—not the stock market, foreign affairs, welfare, terrorism, or even health care."

The poll was conducted November 9-10, 2003 by The Tarrance Group, who surveyed 604 registered voters. Partner Brian Tringali and Senior Research Analyst Brian Nienaber advised The Buckeye Institute on the design, implementation, and analysis of the poll results.

"Ohio's continuing struggle to balance its budget suggests the need for substantial fiscal policy reform," noted Staley in the report. "State policymakers need to focus their efforts on two important and complementary strategies: spending

"State policymakers need to focus their efforts on two important and complementary strategies: spending restraint and fundamental tax reform."

restraint and fundamental tax reform.

"Significant reform in both of these areas would help rationalize state government and provide a fiscal policy framework that would significantly enhance economic growth and restore Ohio's economic competitiveness," Staley concluded.

Joshua Hall is director of research for The Buckeye Institute. His email address is hall@buckeyeinstitute.org.

INTERNET INFO

The full text of the report, "New Directions for Fiscal Policy in Ohio: Citizen Attitudes Toward Spending and Taxation," is available on The Buckeye Institute's Web site at <http://www.buckeyeinstitute.org>, or by calling 614/224-4422. Tell 'em *Budget & Tax News* sent you!



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Oklahoma Governor Signs \$5.3 Billion Spending Bill

by Sandra Fabry and Paul Proski

While Oklahoma Governor Brad Henry has signed a \$5.3 billion spending bill that appropriates funds for the fiscal year beginning July 1, the tax and spending outlook in Oklahoma City is not yet clear. According to the Associated Press, Henry "said much budget work was still left for lawmakers" to finish.

Taxpayer groups say Henry, a Democrat, is sending mixed messages.

Henry has said, for example, that "The money for important programs is there. It's just a matter of setting priorities and shifting funds to meet them. Legislative leaders have committed to do that, and I will work with them to make sure all of our objectives are realized." At the same time, however, Henry is proposing significant tax increases.

The spending bill Henry approved counts on a tax and revenue increase of \$201 million. On March 8, he signed legislation that authorizes expanded gaming at Blue Ribbon Downs in Sallisaw, Remington Park in Oklahoma City, and Will Rogers Downs in Claremore. According to the thoroughbred industry, the new law could raise \$71 million for Oklahoma's upcoming budget. Henry hopes to generate the rest from a massive cigarette tax increase.

Taxpayer Groups Protest

Taxpayer advocates have criticized Henry's tax increase approach.

Karen Kerrigan, chairman of the Washington, DC-based Small Business Survival Committee, points to the negative implications for Oklahoma's business community. She thinks the tax hike will ultimately backfire. "Small retailers will be hurt by the tax, which means less revenue for the state. Increasing the tobacco tax will simply perpetuate the vicious tax-and-spend cycle that has many states in a bind. Once revenues generated by the tax increase fail to live up to projected levels, small businesses will be targeted again with another misguided tax hike plan."

Taxpayer groups also challenge the rhetoric resorted to by advocates of higher taxes. Says John Berthoud, president of the National Taxpayers Union: "They always try to claim that the money raised from higher tobacco levies is not what they want—allegedly, they are raising tobacco taxes because they want to 'discourage tobacco use.'" Henry has said the tobacco tax increase would fund a vaguely defined "health initiative."



Governor Brad Henry signed legislation intended to raise money by expanding gaming at some of the state's horse race tracks.

Noted Berthoud, "This fable is proven false every time as the politicians—just as they have in Oklahoma—always come up with grand, heart-tugging schemes to spend their new-found loot."

While Henry appears to believe a tax hike is the only way to address the state's fiscal needs, other states have closed budget holes without raising taxes. Colorado, Hawaii, Massachusetts, Minnesota, New Hampshire, and Texas have found alternative solutions to restore fiscal sanity to their budgets. By identifying unnecessary programs and reining in spending, Gov. Rick Perry of Texas was able to shrink the budget below the previous year's level.

"Uncontrollable Spending"

The taxpayer advocacy groups contend the underlying reasons for the state's budget woes are clear—and not addressed by the governor's proposal. "Hiking tobacco taxes as a fix to Oklahoma's budget woes is a harmful solution that does not address the underlying budget problem—uncontrollable spending," explained Kerrigan.

Nationwide, most states spent lavishly during the boom years of the 1990s. Oklahoma was no exception. "After adjusting for inflation and population, spending at the state level increased by significant amounts in recent years," noted economist Raymond J. Keating in a 2003 publication of the Oklahoma Council for Pub-

lic Affairs. "For example, from 1992 to 2000, per-capita state total expenditures in Oklahoma increased by 19.5 percent, while inflation over the same period registered 16.4 percent," he wrote.

As the nation's economy slumped and state government revenues fell, policymakers across the country found themselves unable to meet the spending commitments they had made when coffers were overflowing. For the past few years, states have had to choose between cutting spending to sustainable levels or raising additional revenues with new and increased taxes.

When asked how they would want their elected representatives to address budget shortfalls, voters in state after state have urged spending restraint.

In Virginia and Oregon more than a year ago, tax increases were defeated at the ballot. Last summer, Alabama voters rejected Gov. Bob Riley's tax hikes by a 68 to 32 percent vote. California Gov. Gray Davis was recalled for overspending and tripling the car tax. And just a few weeks ago, Oregon voters rejected another tax increase proposal by a vote of 60 to 40 percent. Petition drives are currently underway to repeal tax hikes in Nevada and Ohio.

"Gov. Henry is proposing tax increases at his own risk," warned Grover Norquist, president of Americans for Tax Reform (ATR).

Message Is Mixed

Henry's advocacy of certain tax cuts has muddled the waters of tax policy in Oklahoma, leaving many to wonder whether a coherent policy can emerge. According to the governor's Web site, Henry favors the elimination of all capital gains taxes on Oklahoma-based property, permanent reduction of Oklahoma's top income tax rate to 6.65 percent (from 7 percent), and expansion of income tax relief on pension and IRA distributions for retirees.

Those measures, however, are not enough to offset his proposed tax increases, noted ATR's Norquist.

"If Gov. Henry looks to the example of President Bush and sees the benefit of cutting tax rates, why is he stopping at such small cuts? If he believes health programs should be paid for by tobacco taxes, and if he believes that capital gains and income tax cuts are good for Oklahoma, then he should expand the tax cuts to offset fully the tobacco tax hikes he is pushing.

"If he refuses to do so," Norquist concluded, "he is demonstrating that he really just wants more money to spend."

Sandra Fabry is an associate for state government affairs, and Paul Proski is state government affairs manager, with Americans for Tax Reform. Their email addresses are sfabry@atr.org and pproski@atr.org, respectively.

STATE UPDATE

Kansas Fiscal Battle Continues

by Karl Peterjohn

Elected officials in Kansas have spent the first months of the 2004 session trying to put the state's fiscal house in order. As of this writing, no end to the tug-of-war is in sight.

The state senate voted 14-25 against Governor Kathleen Sebelius's tax hike proposal on February 26, and on April 1 it rejected two proposals to raise taxes for school finance. But on March 26, the Kansas House passed on a 72-52 vote a large package of tax hikes and provided much broader local property tax authority for local school districts.

On March 30, *the Lawrence Journal World* reported, "House and Senate negotiators agreed on a budget that trims state spending by three-tenths of 1 percent [from last year], settling dozens of small issues but leaving big ones unresolved. Leaders expect decisions on those services [education and transportation spending] to be made just before the session ends in early May." Tax increases are still on the table in Kansas.

Sebelius sought an increase of 10 percent in the state's property tax for schools, a 5 percent income tax surcharge on personal incomes, and an increase of .7 cents in the state's permanent sales tax rate of 5.0 percent. The

current, temporary statewide sales tax rate is 5.3 percent.

Business Leaders Comment

Business leaders in Kansas joined tax policy analysts nationwide in recommending against the Sebelius proposal.

"Regrettably, there are unfortunate financial implications for the economy

"Instead of raising taxes, Kansas should be taking the initiative to become a competitive leader among states in the fight for jobs."

LEW EBERT

of Kansas if this proposal is ever funded in the manner that has been suggested," warned Lew Ebert, president and CEO of the Kansas Chamber of Commerce. "Consequently, the Kansas Chamber of Commerce will resist the increase in sales taxes, the increase in property taxes, and the increase in income taxes contained in this proposal."

Ebert urged lawmakers in early February to take whatever actions were pos-

sible to lower the cost of doing business in Kansas and improve the state's climate for new and expanding businesses. Increasing income, property, and sales taxes, Ebert said, would hurt citizens in general and small businesses in particular.

"Instead of raising taxes, Kansas should be taking the initiative to become a competitive leader among states in the fight for jobs," Ebert said. "We can improve our competitive position. We must improve our competitive position. We are in a fight for new jobs and to keep the jobs we still have in Kansas."

Paul Gessing, director of government affairs for the Washington, DC-based National Taxpayers Union, echoed Ebert's concern for the state's economy.

"When fully implemented, [the governor's] tax increase would have a \$450 million annual price tag," Gessing noted. "The tax hikes would cost Kansas more than 3,700 jobs and would reduce its gross state product by more than \$200 million, thus reducing investment and income in the state as well."

The state legislature is scheduled to adjourn its 2004 session in early May. But before it can do so, it must get a budget passed ... and the final budget document is not expected to be ready for debate before the end of April at best.



Governor Kathleen Sebelius

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INTERNET INFO

For more information visit the Web site of the Kansas Taxpayers Network at <http://www.kansastaxpayers.com>.

Kansas Lawmakers Reject School Finance Myths

by Karl Peterjohn

On March 11, the Kansas House of Representatives rejected a \$1 billion tax hike proposal for financing the Shawnee Mission school district, which has the second-largest student enrollment in the state.

The vote suggests state legislators may be coming to understand that much of the "conventional wisdom" on state spending in general and school finance in particular is wrong. Most lawmakers were not swayed by heavy lobbying from school spending growth advocates at the statehouse.

But on April 6, Shawnee Mission voters approved a \$184 million bond issue by a 2-to-1 margin, suggesting myths continue to pervade the school finance debate. What follows are four prominent myths that have often held sway.

Myth 1: State spending for K-12 is inadequate.

Total spending for K-12 education in Kansas for the first time exceeded \$9,000 per pupil last year. Enrollment in Kansas public schools, which peaked about five years ago, has been falling since and is now at best flat. The total tax expenditure on Kansas public schools now exceeds \$4 billion a year.

Myth 2: Schools are spending only \$3,863 per pupil.

The \$3,863 per-pupil figure represents the state's spending on base state aid only. Total state spending aver-

ages well over \$5,000 per pupil per year in Kansas; local and federal spending brings that to more than \$9,000.

Myth 3: Kansas school finance is unconstitutional.

A district court judge in Shawnee County has issued a preliminary opinion that the state's system of school finance is unconstitutional. But the Kansas Supreme Court has already ruled on the subject, upholding the constitutionality of the school finance system that has been in place since 1992.

Myth 4: State school spending has not kept up with inflation.

Between 1992 and 2004 state spending on K-12 increased by more than \$1.3 billion, rising from \$1.028 billion to a projected \$2.330 billion. That 126 percent increase is almost four times the rate of inflation during that 12-year period, as measured by the Consumer Price Index.

"The March 11 vote in the legislature was a victory for those of us who believe schools don't need more money," said George Petersen, a taxpayer advocate for Kansas Taxpayers Network. "But we all know tax victories like this can be short-lived. We'll have to stay sharp, because we know the tax-and-spend crowd didn't give up on April 6."

Karl Peterjohn is executive director of the Kansas Taxpayers Network. His email address is kpeterjohn@prodigy.net.



States Spend Tobacco Settlement on Budget Shortfalls

by Christine Hall

More than half (54 percent) of the funds states will receive this year from companies bound by the 1998 tobacco settlement will be spent patching state budget shortfalls, according to a report released March 22 by the U.S. General Accounting Office (GAO).

Just 2 percent of the funds will go toward tobacco control (anti-smoking) efforts, reported the GAO. Seventeen percent will go to health-related programs, 7 percent to debt service on securitized funds, 6 percent to general purposes, and 5 percent to infrastructure.

The report, *Tobacco Settlement: States' Allocations of Fiscal Year 2003 and Expected Fiscal Year 2004 Payments*, documents how states are spending the proceeds of their long-term tobacco settlement money. States expect to receive \$11.4 billion in fiscal year 2004 as a result of the settlement.

The Farm Security and Rural Investment Act of 2002 (the 2002 Farm Bill) requires GAO to report annually on payments made by tobacco companies for fiscal years 2002 through 2006 and how states use these funds.

Shifting Priorities

The March report is the third GAO has released under the Farm Bill mandate. The first report (covering fiscal years 2000-2001) did not collect data on settlement funds spent for budget shortfalls and debt service. But the GAO has found spending of tobacco settlement funds for those pur-

poses has increased dramatically since 2002, while spending for health care and tobacco control programs has fallen.

In 2002, 22 percent of tobacco settlement funds were allocated to budget shortfalls and debt service; in 2004, the GAO projects that figure will reach 61 percent. By contrast, in 2002 health and tobacco control efforts were allocated 40 percent of the settlement funds; in 2004 they will get just 19 percent. (See accompanying figure.)

Notes the GAO report, "States allocated the largest portions of their fiscal year 2003 tobacco settlement funds to address budget shortfalls and for health-related programs, and states expect the same to hold true for fiscal year 2004. Overall, the portion of allocations going to budget shortfalls has been increasing and the portion going to health costs has been decreasing."

The 1998 Master Settlement Agreement (MSA) between 46 state attorneys general and the four major tobacco companies does not require states to spend settlement money on treating smoking-related illnesses. But many state officials, then and more recently, claimed a commitment to do so.

When the MSA was signed, the attorneys general and plaintiffs lawyers held news conferences touting how the money would be used for public health and protecting kids. Washington Attorney General Christine Gregoire said, "Washington state's proceeds from the tobacco industry settlement should be spent on public

health issues or the integrity of the historic agreement will be violated."

The GAO report shows Washington allocated roughly 20 percent of its 2003 tobacco settlement funds for health and tobacco control purposes. In 2004, the GAO projects Washington will allocate nearly 75 percent for those purposes. As is true in most states, however, much of the health spending is unrelated to smoking, going to such programs as children's Medicaid and immunization programs.

Unkept Promises

"The \$240 billion settlement was sold to the American people as compensation for treating smoking-related illnesses, but it's the states that have become addicted to tobacco money, spending it on all kinds of [unrelated] programs," said Sam Kazman, general counsel for the Washington, DC-based Competitive Enterprise Institute.

"State attorneys general and anti-tobacco activists at the American Legacy Foundation want smokers, who bear the brunt of the cost of the settlement, to pay for multimillion-dollar anti-smoking ads," said Kazman. "But it turns out that states themselves are spending very little of their tobacco settlement money on tobacco control."

"Trial lawyers were awarded an estimated \$10 to \$30 billion from the settlement. If anti-tobacco campaigns are so important, why can't they cough up a few million for the cause?" he asked.

Tobacco companies also noted the settlement money was intended to fund anti-

smoking efforts.

R.J. Reynolds points out on its Web site, "Although the [Master Settlement Agreement] repeatedly mentions 'implementation of tobacco-related public health measures,' each state decides how its MSA funds are spent. Tobacco companies do not have any input into how the states spend their settlement funds."

"R.J. Reynolds Tobacco Company believes that states should take advantage of having unprecedented funds available to combat youth smoking, and that a significant portion of the states' payments should be spent on preventing tobacco use among minors."

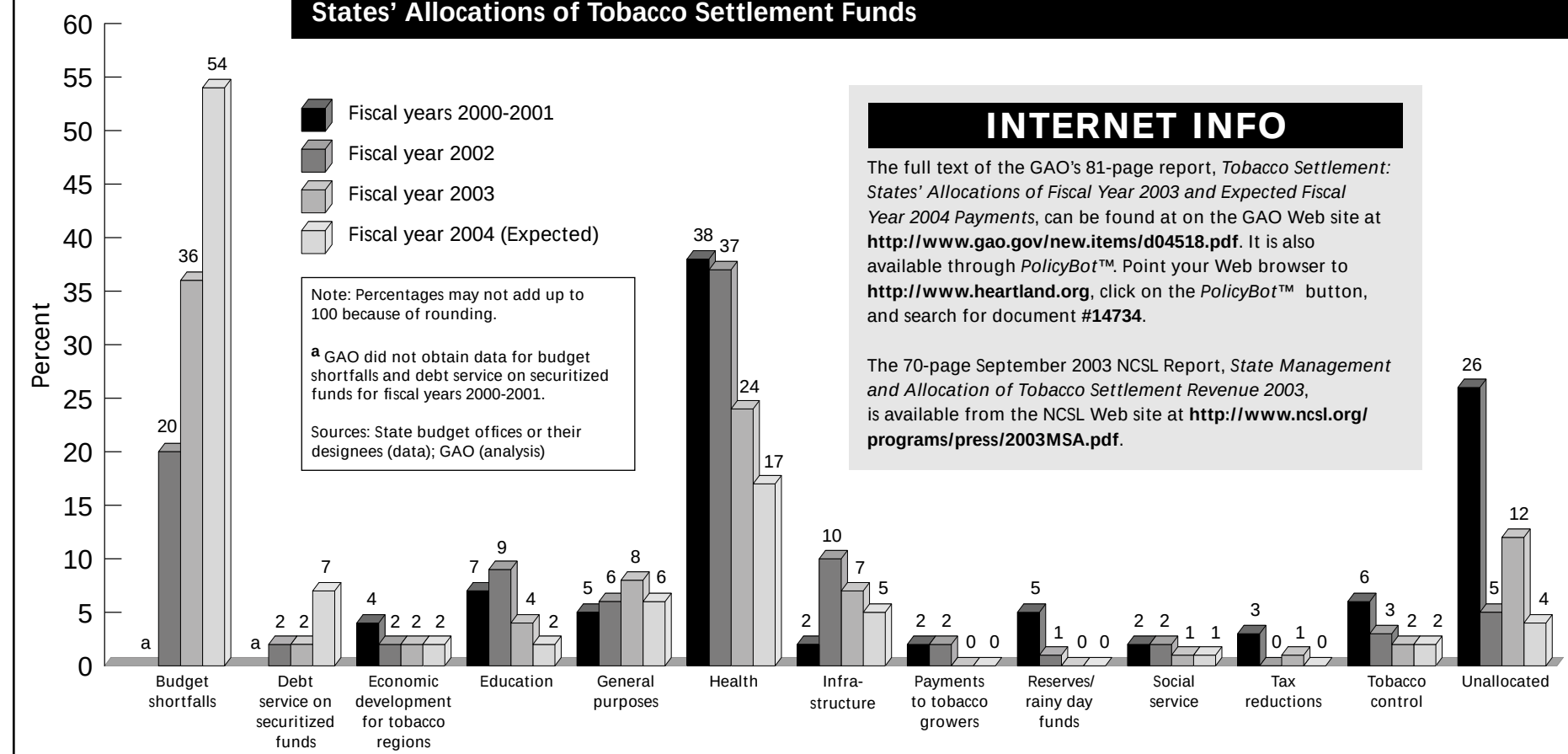
The Centers for Disease Control and Prevention (CDC) has recommended that 20 to 25 percent of the MSA payments go toward smoking prevention programs.

By the end of 2001, states had received more than \$13.4 billion in MSA payments. Only seven states—Arizona, Indiana, Maine, Massachusetts, Mississippi, Ohio, and Vermont—had met or exceeded the CDC's recommendation.

The National Conference of State Legislatures (NCSL) analyzed state plans for spending MSA funds during fiscal years 2000 through 2003. Of the total \$33.1 billion in MSA funds states received during that period, more than half of the money was found to be earmarked for projects unrelated to smoking.

Christine Hall is director of research for the Competitive Enterprise Institute. Her email address is chall@cei.org.

States' Allocations of Tobacco Settlement Funds



INTERNET INFO

The full text of the GAO's 81-page report, *Tobacco Settlement: States' Allocations of Fiscal Year 2003 and Expected Fiscal Year 2004 Payments*, can be found at on the GAO Web site at <http://www.gao.gov/new.items/d04518.pdf>. It is also available through PolicyBot™. Point your Web browser to <http://www.heartland.org>, click on the PolicyBot™ button, and search for document #14734.

The 70-page September 2003 NCSL Report, *State Management and Allocation of Tobacco Settlement Revenue 2003*, is available from the NCSL Web site at <http://www.ncsl.org/programs/press/2003MSA.pdf>.

STATE UPDATE

California

Continued from page 1

"The Blank Check Initiative [Prop 56] would have eliminated the most important protection taxpayers have against unjustified state tax increases—the two-thirds legislative vote required before Sacramento can raise our taxes," said Larry McCarthy, president of the California Taxpayers' Association.

Had Prop 56 passed, tax and appropriations bills would have required the approval of only 55 percent of legislators.

Business Leaders Reject Measure

The California Chamber of Commerce led a business community effort to defeat Prop 56, marshaling a broad-based coalition that ran ads and mobilized voters.

"We all thank the California State Chamber for immediately recognizing the threat this proposition posed to taxpayers and jobs, and for successfully leading the coalition that defeated it," said Peter Cressy, president of the Distilled Spirits Council (DISCUS).

The California Restaurant Association, Family Winemakers of California, and California Lodging Industry Association were also among the hospitality

industry groups joining the Chamber-led coalition.

"Had this initiative passed," Cressy continued, "there is no doubt that the hospitality industry in California would have been subjected to extremely onerous job-killing taxes. This is a victory for beer, wine, and spirits as well as the wholesalers, restaurateurs, and other retailers who came together to spearhead the fight against this labor-backed initiative."

DISCUS and its member companies, along with beer and wine distributors and other sectors of the hospitality industry, raised \$2.9 million to fight the initiative. The Chamber-led coalition together raised approximately \$10 million. Proponents of the initiative, primarily government employee labor unions, spent more than \$15 million in their unsuccessful effort to pass the measure.

The Chamber of Commerce-led effort was bolstered by the efforts of taxpayer, small business, public safety, and senior advocacy organizations. Among the groups that formally announced their opposition to the measure and worked toward its defeat were the California Taxpayers' Association, Howard Jarvis Taxpayers Association, Sacramento County Taxpayers League, National Tax Limitation Committee, California Taxpayer Protection Committee,

Alliance of Contra Costa Taxpayers, Contra Costa Taxpayers Association, California State Sheriffs' Association, California State Automobile Association, California Farm Bureau Federation, Small Business Survival Committee, The Seniors Coalition, 60 Plus Association, and the National Federation of Independent Business.

Accountability Smokescreen

The proponents of Prop 56 contended it would make it easier to pass the state budget, which is often the subject of wee hours-debate and political deal-making. Passing budgets on time, they argued, would ease the financial worries of state programs and employees and would also help improve the state's credit rating. Moreover, proponents noted, a 55 percent requirement is higher than what is required in 47 other states.

Opponents responded that Prop 56 would have made it easy not only to pass budgets, but to pass tax increases as well. They referred to it as the "blank check initiative" and the "take my wallet, please" initiative. Carol Evans, vice president of the California Taxpayers Association (CTU), warned, "giving even more money to the same people who've spent us into a deficit already, by making it easier for politicians to raise our taxes—that's like giving an alcoholic free run of the bar."

While it may be a good thing to get state budgets passed on time, opponents argued, budgets with tax increases are not a good thing.

"The proponents are running misleading ads—talking about accountability and on-time budgets—but voters must know that Proposition 56 is a very deceptive measure," said Jim Goodwin, president and CEO of the Chico Chamber of Commerce.

"It pretends to hold the politicians accountable, when it actually rewards them with an open-ended blank check," charged Goodwin. "It would give them a free hand to increase our sales taxes, income taxes, property taxes, and other

state taxes, year after year, without justification or any bipartisan consensus."

Tod Kimmelshue, board member of the California Farm Bureau Federation, joined Goodwin. "People in this region know that agriculture operates on a tight margin," said Kimmelshue. "These days, we compete with each other, with other parts of the state, with other states, and even with other countries. And what's true for agriculture is true for many other businesses around the state."

"Do we really want to make it easier for Sacramento politicians to raise our taxes?" asked Kimmelshue. "The answer from agriculture and small business today is No. We need real accountability in Sacramento, and Prop. 56 doesn't deliver it."

Groundswell in Opposition

Even before the final vote, state surveys indicated Prop 56 was in trouble. In a late January poll released by the Public Policy Institute of California, 73 percent of likely voters said it is a good idea to require a two-thirds vote to pass the budget. "It's not that Californians have been stingy when it comes to paying taxes," said the CTU's Evans. "State taxpayers are already ponying up to the tune of \$130 billion in state and local taxes each year."

Lew Uhler, president of the Roseville, California-based National Tax Limitation Committee, told a rally just before election day, "Prop. 56 pretends to discipline politicians with one hand, but instead rewards them with an open-ended blank check to increase taxes year after year."

"Make no mistake," Uhler warned, "that's the real aim of Prop. 56, and that's exactly what we'll get if Prop. 56 passes: higher income taxes, sales taxes, and property taxes."

Two-thirds of the state's voters apparently heard that message, loud and clear.

John Skorborg is managing editor of Budget & Tax News. His email address is skorborg@heartland.org.

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California Proposition 56

Defeated by voters on March 2
66 percent to 34 percent vote

Official Title and Summary
Prepared by the Attorney General
State Budget, Related Taxes, and Reserve.
Voting Requirements. Penalties. Initiative
Constitutional Amendment and Statute.

- Permits Legislature to enact budget and budget-related tax and appropriation bills with 55% vote rather than 2/3 vote currently required.
- Requires that Legislature, Governor permanently lose salary, expenses for each day budget is late.
- Requires that Legislature stay in session until budget is passed.

- Requires budget summary in state ballot pamphlet and link to Internet website with legislators' voting records on budget and related taxes.
- Requires 25% of certain state revenue increases be deposited in reserve fund, which cannot be used to increase spending.

Summary of Legislative Analyst's Estimate of Net State and Local Government Fiscal Impact

- This measure would have varying state fiscal impacts from lowering the legislative vote requirement for budget-related spending and tax increases—including changes in spending and potentially significant increases in state tax revenues in some years. Fiscal impacts would depend primarily on the composition and actions of future Legislatures.

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Maine Taxpayers Favor Property Tax Cap

by John Skorburg

In a recent statewide poll, a majority of Maine taxpayers expressed support for a statewide mandate to cap local property taxes. A referendum on the ballot later this year will give voters an opportunity to vote on the plan.

According to a March 10 AP report, "More than half [51 percent] of the Maine voters surveyed said they would vote for, or lean toward, a plan to limit taxes to 1 percent of the assessed value of a property."

The random survey of 400 registered voters was conducted between February 28 and March 3 as part of the quarterly Omnibus Poll by Strategic Marketing Services. Less than one-third of the surveyed voters said they would vote against the cap or lean toward doing so, while 18 percent were undecided.

"I think the question straight up probably reads very well—who doesn't want to cut their taxes?" said Patrick Murphy, president of Strategic Marketing Services. "When all the issues come out then there'll be a spirited debate and then who knows how it will go."

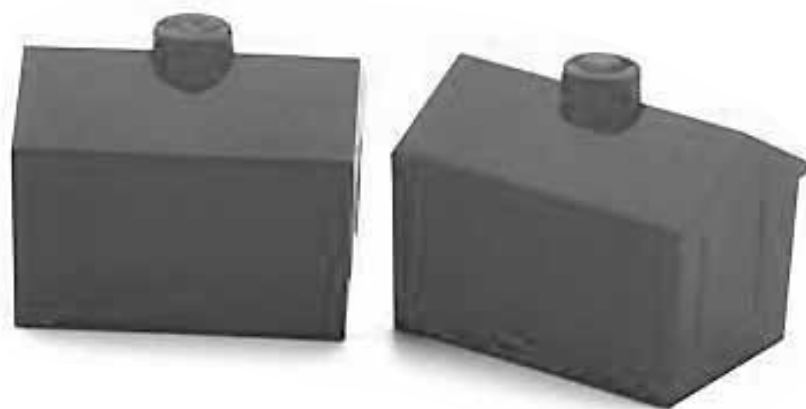
According to a March 11 report in the *Portland Press Herald*, the referendum will

be held in June or November of this year.

The initiative would, with some exceptions, limit property taxes to 1 percent of a home's assessed value. The cap would allow a higher tax rate if a community had certain voter-approved debt. The plan also would roll back assessed property values to the 1996-97 level and cap assessment increases, allowing an annual adjustment of no more than 2 percent.

The property tax cap plan is the brainchild of Carol Palesky and her Maine Taxpayers Action Network (MTAN). Talking to a local ABC affiliate, the 63-year-old Palesky said the number of MTAN followers swelled from 2,000 to more than 25,000 during a two-week period in February, when the tax cap plan began attracting attention. Palesky said she gets "50 to 75 e-mails a day," and that a man gave her a \$5,000 check after she spoke to a chamber of commerce breakfast meeting recently in Portland.

Palesky is considered a maverick by many of the local politicians. The Maine Municipal Association, which predicts the referendum would lead to a 40 to 60 percent cut in property tax revenues, opposes her plan.



Palesky has said municipal officials are exaggerating the impact of the tax cap proposal to scare voters. Most towns and cities run surpluses and overspend on administration, she said. Palesky recently told the *Sun Journal* of Lewiston she would "eat her hat" if the measure doesn't pass.

Former Republican State Senator Phil Harriman of Yarmouth, who supports the tax cap, said the poll results "send a message to the Legislature that people are upset about high property taxes and are demanding tax reform." Harriman served in the Senate from 1992 until 2000 and sat on the Appropriations and Financial

Affairs Committee during his final term.

"It speaks to the fact that there is a lot of pent-up frustration and that our elected leaders in Augusta are not hearing the message," Harriman said. "I sure hope the Legislature will take the opportunity to lead and bring forth something that is meaningful." He told the *Portland Press Herald* he "plans to play an active role in promoting the tax cap to stand up for people who are struggling to pay their property taxes."

John Skorburg is managing editor of Budget & Tax News. His email address is skorburg@heartland.org.

How to Reduce Revenue Instability

Oregon would benefit by dropping its capital gains tax

by Michael L. Barton

The proponents of new or different taxes in Oregon claim the income tax is "unstable because it produces excess revenue in boom times and shows sharp declines in times of recession." That is undeniably true.

The aggregate income of Oregonians from which the income tax is extracted does show sharp swings, according to Oregon Department of Revenue data.

However, a closer look at the same data reveals a solution to that problem. The solution involves neither income tax surcharges, like that passed by the Oregon legislature but trounced by voters in Measure 30, nor new taxes of the sales or other varieties.

According to the report *Oregon Personal Income Tax Statistics Tax Year 2001*, published by the Oregon Department of Revenue, in the boom years between 1990 and 2000 the adjusted gross income of Oregonians increased an average of 7.4 percent each year. The taxes on this income

poured into Salem at the same rate. Then in 2001 the stock market fell, the recession hit, and gross income fell 4.4 percent, accompanied by a similar drop in tax revenues.

Here is the interesting thing. Dur-

"Since the stated goal of the tax reformers is to narrow the swings in state revenue, let's see what happens if we leave capital gains out of the equation."

ing the '90s one component of income rose much faster than others, and then fell most dramatically in 2001. That was capital gains income, which rose at an average rate of 17.6 percent between 1990 and 2000 and then fell 51.3 percent in 2001.

Stabilizing Revenue

Since the stated goal of the tax reformers is to narrow the swings in state revenue, let's see what happens if we leave capital gains out of the equation.

We find that between 1990 and 2000, the remaining aggregate income rose at a strong 7.0 percent per year. In 2001, rather than falling sharply, the income figure holds essentially level, actually increasing a bit.

So here is a modest proposal to stabilize revenues for Oregon state government: Repeal the income tax on capital gains. That one simple change will resolve most of what the critics claim is wrong with Oregon's tax system.

Want a stable funding source for schools? Absent the tax on capital gains, the schools could have weathered the recent recession in decent shape. Revenue would have grown rapidly (perhaps too rapidly) in the 1990s, but would not have dropped

when the recession hit. Surely the schools can tolerate flat funding at times when the overall income of Oregonians is dropping.

Repeal of the capital gains tax would have the additional benefit of being good for Oregon's economy. The business activity reflected in capital gains—the buying and selling of assets—is what causes wealth and job creation. By removing the tax on this activity we will see more of it ... just what we need in hard times.

Michael L. Barton, Ph.D., is an academic advisor to Cascade Policy Institute, a Portland, Oregon think tank. His email address is info@cascadepolicy.org.

INTERNET INFO

For more information visit the Cascade Policy Institute's Web site at <http://www.cascadepolicy.org>.

STATE UPDATE

Smokers Oppose Kentucky Governor's Tax Plan

by John Skorburg

Reporter Kate Scott of KFVS Channel 12 in Kentucky got an earful from Bluegrass State smokers when she asked how they felt about Governor Ernie Fletcher's proposed cigarette tax increase.

"I don't like it," declared Rodney Myatt of Kevil.

"I think it's unfair," Greg Majors of Barlow mourned. "It's just another dent in your paycheck."

Scott reported, "Right now, Kentucky's cigarette tax is the second-lowest in the nation, at just three cents per pack. It's a price break that draws smokers to Kentucky from neighboring states, especially Illinois, where the tax is nearly a dollar per pack."

"But Governor Fletcher wants to bring the tax in the Bluegrass State up to 29 cents per pack. That would put Kentucky's cigarette tax higher than both Missouri's (17 cents) and Tennessee's (20 cents)."

Some people say the governor's plan will backfire, making the state lose revenue by sending smokers somewhere else. "A lot of people come here to buy cigarettes in Kentucky because of the low prices. If

they raised [taxes], I'd have to try to find another state to buy cigarettes in," said Majors.

Not all Kentuckians, however, are opposed to the plan.

"It doesn't really matter to me, because I don't really smoke," said Shirley Dykes of LaCenter. "I guess it would be to other people that did smoke. But if it would help the state, I would go along with it."

Showing a keen sense of the politics involved, W.E. Hixon of Arlington declared, "If the state needs the money, I think the cigarette tax is a good place to get it, rather than gasoline. You know, gasoline is going to be high enough already. So I say, lay it on the smokers."

Just let 'em try, vowed smoker Jason Donelson of Kevil. "If cigarettes are cheaper right over the bridge, I'll go right over the bridge and buy them. If they're cheaper five miles down the road, I'll go five miles down the road," he said. "And anybody else would be stupid not to."

John Skorburg is managing editor of Budget & Tax News. His email address is skorburg@heartland.org.



"If cigarettes are cheaper right over the bridge, I'll go right over the bridge and buy them. If they're cheaper five miles down the road, I'll go five miles down the road."

Kentucky

Continued from page 1

According to the release, Fletcher's Jobs and Opportunity Bipartisan Solution for Kentucky (JOBS for Kentucky) is a "revenue-neutral approach."

"Kentucky has been suffering from a growth deficit for too many years because our current tax system makes it impossible to compete with other states," Fletcher said. "We have been penalizing job creators for setting up shop here and at the same time rewarding businesses for being based in other states."

Grover Norquist, president of the Washington, DC-based Americans for Tax Reform, noted Fletcher has signed the group's "No New Taxes" pledge. "I would like to commend Governor Fletcher on reducing marginal tax rates to make Kentucky's businesses more competitive as well as resisting the demands of special interests to increase [overall] taxes," Norquist said.

Details

The JOBS for Kentucky proposal has been introduced in the state House of Representatives by Scott Brinkman (R-Louisville) and Rep. Robert Damron (D-Nicholasville). Among other things, the measure:

- removes from the income tax rolls any family with an income at or below \$12,000 per year.

- reduces the top personal income tax rate to 5.68 percent from 6 percent. In future years, the top tax rate will drop to as low as 4 percent as growth in state revenues and jobs reach specific triggering targets.

- provides a three-day sales tax holiday prior to the beginning of the school year, during which all purchases of clothing, school supplies, and computers would be exempt from sales and use tax.

- reduces the maximum corporate income tax rate to 6 percent from 8.25 percent.

- increases the cigarette tax nearly 900 percent, from 3 cents to 29 cents per pack.

- imposes a statewide lodging tax of 1 percent of the room charge.

- broadens the corporate tax base to include limited liability entities.

- eliminates excise taxes and the case tax on alcoholic beverages, replacing them with a revised wholesale tax.

- establishes a communications excise tax of 7.62 percent on cable and satellite television providers.

"Some people mistakenly think tax modernization is just another way to raise revenues through tax increases," said Fletcher. "Let me be clear: Any growth in revenue for the state will result from economic growth and creation of new jobs, not higher taxes."

Driven by Economic Growth

Reporters for Cincinnati.com, the *Cincinnati Enquirer's* online edition, accepted Fletcher's explanation that,



Governor Ernie Fletcher

under his plan, state revenue growth would come only from economic growth. "Fletcher's plan is, in fact, driven by a belief that cutting income and business taxes will stimulate economic growth and eventually lead to more state revenue, not less, by creating more taxpayers," the newspaper reported.

Fletcher's plan is based on the "dynamic scoring" approach of supply-side economics—an assumption that a change in tax policy will have a broad effect on economic behavior. "Fletcher has taken a page from President Bush in this respect," noted Cincinnati.com.

"Fletcher's approach is the opposite of 'static scoring,' an assumption that a reduction in a given tax will simply yield a reduction in revenues from that tax. No change of behavior is assumed."

"Static scoring will underestimate the revenues you will get from lowering high tax rates," said Paul Coomes, a University of Louisville economist who has been following developments in Frankfort. "There certainly will be changes in behavior. The tough part is, how much?"

Coomes said he was enthused by Fletcher's original plan, which was to slash the top individual income tax rate to 4.9 percent.

"I think Kentucky has a reputation nationally of being a high-tax place. The only way you're going to change that reputation is to turn the direction of your tax system around in a dramatic way," Coomes said.

Cutting the income tax rate by more than a percentage point "tells the world you are changing the tax system from one that apparently is there to sort of redistribute a lot of money away from successful people," Coomes said.

According to Cincinnati.com, politics made it impossible for Fletcher to stick with his 4.9 percent proposal. To attract support for the overall package, he had to scale back some of his proposed tax increases, mainly the cigarette excise tax, which Fletcher first wanted to raise by 40 cents.

John Skorburg is managing editor of Budget & Tax News. His email address is skorburg@heartland.org.

Medicare

Continued from page 1

of the baby boomers will spell fiscal doom for older and younger generations alike.”

“Medicare’s own trustees have confirmed what taxpayer advocates warned about all along,” agreed John Berthoud, president of the National Taxpayers Union (NTU). “A 35 percent increase in the drug plan’s 10-year cost estimate, mounting evidence that employers will dump seniors’ private coverage, and now [the] trustees’ report all add up to an economic doomsday scenario that thoughtful policymakers can’t ignore any longer.”

Berthoud noted full federal drug coverage will go into effect in 2006, thus “lawmakers have only a limited amount of time to prevent what could be the biggest fiscal disaster in U.S. history.”

“Turn for the Worse”

Despite President George W. Bush’s promise that any new Medicare legislation would strengthen the program’s long-term financial security, Medicare’s finances have “taken a major turn for the worse,” according to the trustees’ report. The seven-year adjustment is the largest lurch toward projected insolvency in the program’s 39-year history. Congressional efforts to reduce health care costs are failing miserably, meaning higher premiums for Medicare patients

in the near future.

“Congressional attempts at lowering health costs completely miss the mark,” Schatz noted. “They try to import foreign price controls and regulate eating habits when they should be reversing the government’s disastrous intrusion into the health care system.”

The trustees’ report said changes to the law account for two years out of the seven-year acceleration toward fiscal insolvency.

“In 1965, Medicare was predicted to cost \$26 billion in 2003; the actual cost that year was \$245 billion. Medicare’s unfunded liability currently hovers around \$40 trillion.”

The prescription drug benefit is not included in the trustees’ estimate because it will be funded out of general revenue, not the hospital trust fund that is the main focus of the trustees’ report. Instead, the trust fund will be hurt by other parts of the Medicare reform law, such as subsidizing finances of doctors and hospitals in rural areas. Over the next 75 years, Medicare will have an unfunded liability of \$27.7 trillion, \$8.1 trillion of that from the new drug benefit.

“Today’s politicians are raiding the paychecks of the unborn to impress senior citizens before the 2004 elec-

tions,” Schatz charged. “In the last four months, the bill’s cost rose from \$400 billion to \$534 billion. Imagine what the cost will be 10 years from now!”

In 1965, Medicare was predicted to cost \$26 billion in 2003; the actual cost that year was \$245 billion. Medicare’s unfunded liability currently hovers around \$40 trillion.

A number of short-term problems plague the massive entitlement program. The program that pays for doc-

price controls.”

Such an approach would include expanded Health Savings Accounts for individuals (one of the only positive features in the recently passed reform measure), equal tax treatment for health insurance purchased outside of one’s employer, and tax credits for the uninsured.

“Fifteen years ago, Congress pulled America back from the fiscal abyss when it repealed the flawed Catastrophic Care law before it could exact a terrible toll on seniors and taxpayers,” NTU’s Berthoud concluded. “Now policymakers should draw upon this historical lesson to protect America from the \$8 trillion mistake of a federal prescription drug entitlement.”

Tom Schatz is president of Citizens Against Government Waste. His email address is tschatz@cagw.org.

INTERNET INFO

For more information about Citizens Against Government Waste, visit its Web site at <http://www.cagw.org>.

For more information about the National Taxpayers Union, including its research and writing opposed to the prescription drug entitlement, visit its Web site at <http://www.ntu.org>.

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FEDERAL BUDGET

Weight Loss Plan for Fed

by **Sonia Hoffman**

The federal budget could easily slim down with a workout in the gym of spending cuts and continued economic growth, according to a nine-step weight loss plan published on January 13 by the Lewisville, Texas-based Institute for Policy Innovation (IPI).

"If there is any overriding theme of the economic and fiscal policy-making scene in Washington over the past two decades, it might be this: We fought a war against big government, and big government won," said Stephen Moore, author of the report.

"In just the past three years," Moore continued, "the federal budget has exploded in size by more than one half trillion dollars.

"The sudden spurt of government spending and the resulting mountainous budget deficits are all the more unexpected given that they have occurred under a Republican Congress and president," noted Moore. "After seven budgets designed by the majorities in the House and Senate, the budget is bulkier than ever before. The 108th Congress is spending at a faster pace than any

Congress since before Woodstock."

In "Putting Taxpayers First: A Federal Budget Plan to Benefit the Next Generation of American Taxpayers," Moore spells out specific steps to cut federal spending and put the federal budget on a "glide-path" toward an unprecedented era of prosperity for American taxpayers. The study, according to Moore,

"If there is any overriding theme of the economic and fiscal policy-making scene in Washington over the past two decades, it might be this: We fought a war against big government, and big government won."

STEPHEN MOORE

"offers a nine-step budgetary weight loss plan that protects the financial future of tomorrow's taxpayers."

Moore recommends linking the crusade for a streamlined government with pro-growth tax cuts and debt retirement to benefit future generations. He prescribes budget reforms calculated to appeal to fiscally conservative Republicans and Democrats alike.

Moore's plan would reduce the size of government by more than two-fifths over the next 10 years. The FY 2011 federal budget would be \$1.5 trillion under Moore's plan—nearly half its projected size of \$2.6 trillion.

The plan is far-reaching—even radical—acknowledged IPI President Tom Giovanetti.

"Are [legislators] now claiming that everything the Federal government does—every program, every department, every bureaucracy—is absolutely necessary and immune from consideration?" Giovanetti asked, though he knows full well the answer. "If so, this is a radical and new position for [most] Republicans to espouse."

As far as voters are concerned, howev-

er, Moore said the plan is not at all radical. "By two-to-one margins Americans still say they prefer less government services and lower taxes to more government and higher taxes. Two-thirds of voters consistently say they think their taxes are too high, not too low.

"The goal of government downsizing is not flawed, but the game plan has been," he explained. "For one thing, budget-cutters have not made an effort to garner bipartisan support. Furthermore, they have failed to convince the public that there is a financial and freedom dividend from smaller government."

Finally, Moore noted there is precedent for such far-reaching reform in the U.S. "Starting in the mid-1980s, America's private industries restructured themselves, sweated out inefficiencies, cut costs, and raised productivity levels. The only industry that has been immune from this productivity revolution has been government itself."

Sonia Hoffman is director of media and legislative affairs for the Institute for Policy Innovation. Her email address is shoffman@ipi.org.

Putting Taxpayers First

by **Stephen Moore**

1 Eliminate unnecessary and wasteful programs. The federal budget currently consists of several thousand line item agencies, bureaus, offices, and grant programs. Over the past 20 years very few of these programs have actually ceased operation. Since 1996, not a single federal program of any fiscal consequence has actually been eliminated.

2 Privatize federal assets, using the proceeds for debt retirement. The United States government is bleeding red ink even though it is the wealthiest entity on the planet. The federal government owns almost one-quarter of all the land in the United States. Only a tiny fraction of the vast federal land holdings are of environmental or historical significance; most should be sold to the private sector.

3 Devolve federal programs like education, transportation, and welfare to the states. Our federalist system is based on the sound principle that states should be "laboratories of democracy," and that through competition, experimentation, and innovation states will learn from one another and adopt best policy practices.

4 Replace all federal anti-poverty programs with a more generous Earned Income Tax Credit (EITC) that requires work as a condition of federal assistance. If welfare cannot be fully devolved to the states, a second-best option is to completely abolish all forms of welfare—AFDC, food stamps, public housing, Medicaid, SSI, etc. Part of the savings achieved by abolishing those programs should be used to expand the earned income credit (EIC).

5 Use market-based incentives to fix federal entitlement programs. No plan to downsize the federal government and reduce its costs can possibly succeed

without a strategy for reining in entitlement spending. Federal entitlements now account for well more than half of the budget, and these income transfer programs are by far the fastest growth areas of the federal budget. For years, Congress has treated entitlements as if they were on automatic pilot and their costs were beyond legislative control—this attitude cannot, and need not, continue.

6 Abolish all corporate welfare. America's most costly welfare recipients today are Fortune 500 companies. In 2002 Uncle Sam doled out about \$93 billion in taxpayer subsidies to such firms.

7 Enact legislation to make any American with a net income of more than \$1 million a year ineligible for any form of federal aid. Many federal domestic programs primarily benefit Americans with high incomes. In 1994 the National Taxpayers Union conducted a study pinpointing just what groups get the benefits of federal income transfer programs. The study discovered that Americans with incomes of more than \$100,000 a year account for 5.1 percent of all households, but they receive 5.6 percent of all federal subsidies.

8 Fix federal budget rules to end the inherent bias in favor of spending, rather than saving money and cutting taxes. Congress has done little to change budget rules that skew political decision-making in favor of ever-larger federal outlays. Currently the deck is stacked against those who wish to reduce expenditures. The lesson of the states is that budget rules denying lawmakers the power to spend and tax recklessly can be quite effective deterrents to fiscal irresponsibility.

9 Attach to all spending reduction proposals a tax cut dividend for all taxpayers, as a way to build a taxpayer constituency for spending cuts. A leaner federal budget must be sold to the voters as a means to promote individual liberty and economic freedom. For every dollar they earn, Americans now pay roughly 40 cents to the tax collectors in Washington, their state capital, and city hall—a tax burden incompatible with a free society.

Federal Budget

INTERNET INFO

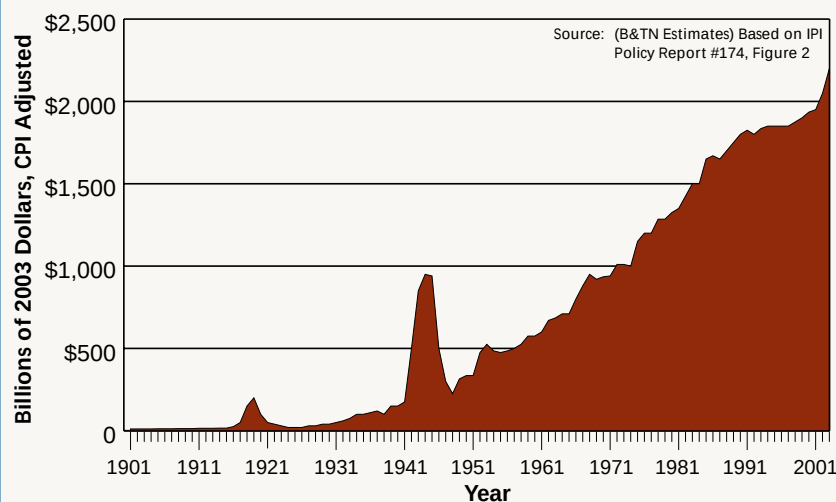
For the full text of Stephen Moore's report, "Putting Taxpayers First: A Federal Budget Plan to Benefit the Next Generation of American Taxpayers," visit the Institute for Policy Innovation Web site at <http://www.ipi.org>.

WHAT \$93 BILLION IN ANNUAL CORPORATE WELFARE SAVINGS COULD BUY

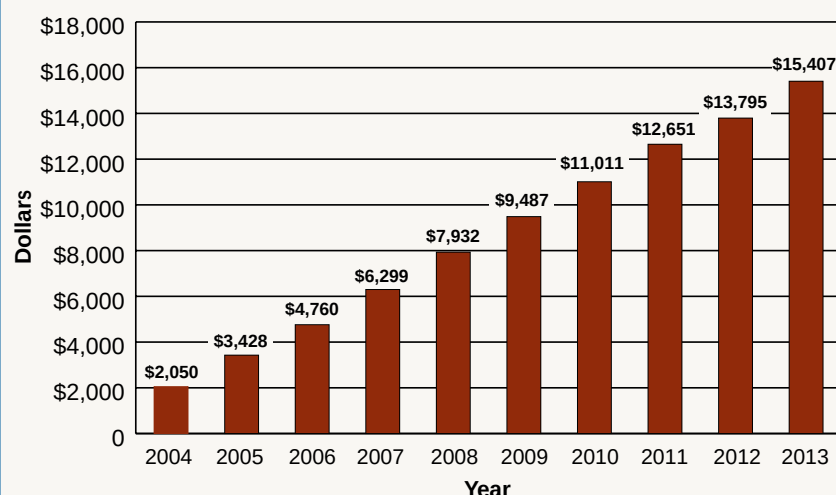
Corporate Welfare Alternatives	Annual Cost
Eliminate Capital Gains Tax	\$65 billion
Eliminate the Death Tax	\$20 billion
Cut Corporate Tax from 35% to 15%	\$82 billion
Cut All Personal Income Tax Rates by 10%	\$85 billion
Establish 20% Flat Tax	\$65 billion
3 Percentage Point Cut in Payroll Tax	\$70 billion

Source: Budget of the United States Government, Fiscal Year 2004

REAL FEDERAL OUTLAYS, 1901-2003



SAVINGS PER HOUSEHOLD FROM IPI WEIGHT LOSS PLAN



Knowing Why Deficit Will Be up Doesn't Take Surplus of Brains

by Terry Savage

Every Presidential election year has its economic themes. In 1992, James Carville famously coined the expression, "It's the economy, stupid!" I'd like to propose a theme for the 2004 election: "It's the spending, stupid!"

The federal budget has gone from a surplus of \$127 billion in 2001 (and a surplus of \$236 billion in 2000) to this year's Congressional Budget Office projection of a \$477 billion deficit—a flip of \$713 billion in just four years.

Congress is now debating next year's budget, which is expected to show a huge increase in both spending and the deficit. Plus Congress is working on a highway bill that adds more than \$256 billion. Politicians of both political parties are trying to buy our votes with our own tax dollars.

But don't blame this year's tax cuts for the deficit. The tax cuts—everything from the top tax rate to the dividend tax cut to the ending of the marriage penal-

ally a surplus in the main Social Security trust funds.

A significant Social Security tax increase, passed in 1983, increased both the percentage of salary paid in FICA and the wage base on which payroll taxes are paid. That tax increase was supposed to build up surpluses in the trust fund for baby boomers' retirement.

And it worked.

On an accounting basis, there are supposed to be huge surpluses in the Social Security trust fund—about \$152.8 billion in 2003, and a combined total surplus of \$1.5 trillion over the past 20 years.

But don't count on seeing that money in your Social Security check when you retire. All of that surplus has been borrowed out of the fund to offset the federal budget deficits we've been running. That practice started in 1983 and has continued every year—even when the federal budget showed a surplus.

All that money in the Social Security

"On an accounting basis, there are supposed to be huge surpluses in the Social Security trust fund ... [But all] of that surplus has been borrowed out of the fund to offset the federal budget deficits we've been running."

ty and increasing the child credit—lowered tax receipts by only \$164 billion this year. The rest of that \$477 billion deficit is being created by new spending.

And don't blame the Iraq war and post-9/11 anti-terrorist measures for all that extra spending. A new study by Brian Riedl of The Heritage Foundation shows that defense spending and all 9/11-related spending amounts to less than half of the increase in government spending last year. The rest comes from a wide variety of programs passed by Congress.

Outrageous Spending

Want some examples of outrageous spending? They're not hard to find. In recent years federal budgets have included money such as \$725,000 for the Please Touch Museum in Philadelphia; \$200,000 for the Rock and Roll Hall of Fame in Cleveland; \$26,000 for a tattoo-removal clinic; and \$293,000 to combat "goth culture" (kids dressing in black) in Blue Springs, Missouri. The list goes on.

These are programs pushed by both political parties, but obviously the voters aren't getting the message. And those cute little projects don't include the estimated \$8.1 trillion future un-funded cost of the Medicare drug-benefit bill over the next 75 years.

You'd never know it, but there's actu-

trust fund has been borrowed, and spent. When they open that great Social Security shoebox as the baby boomers retire, they'll find it's stuffed full of IOUs.

Spending Our Future

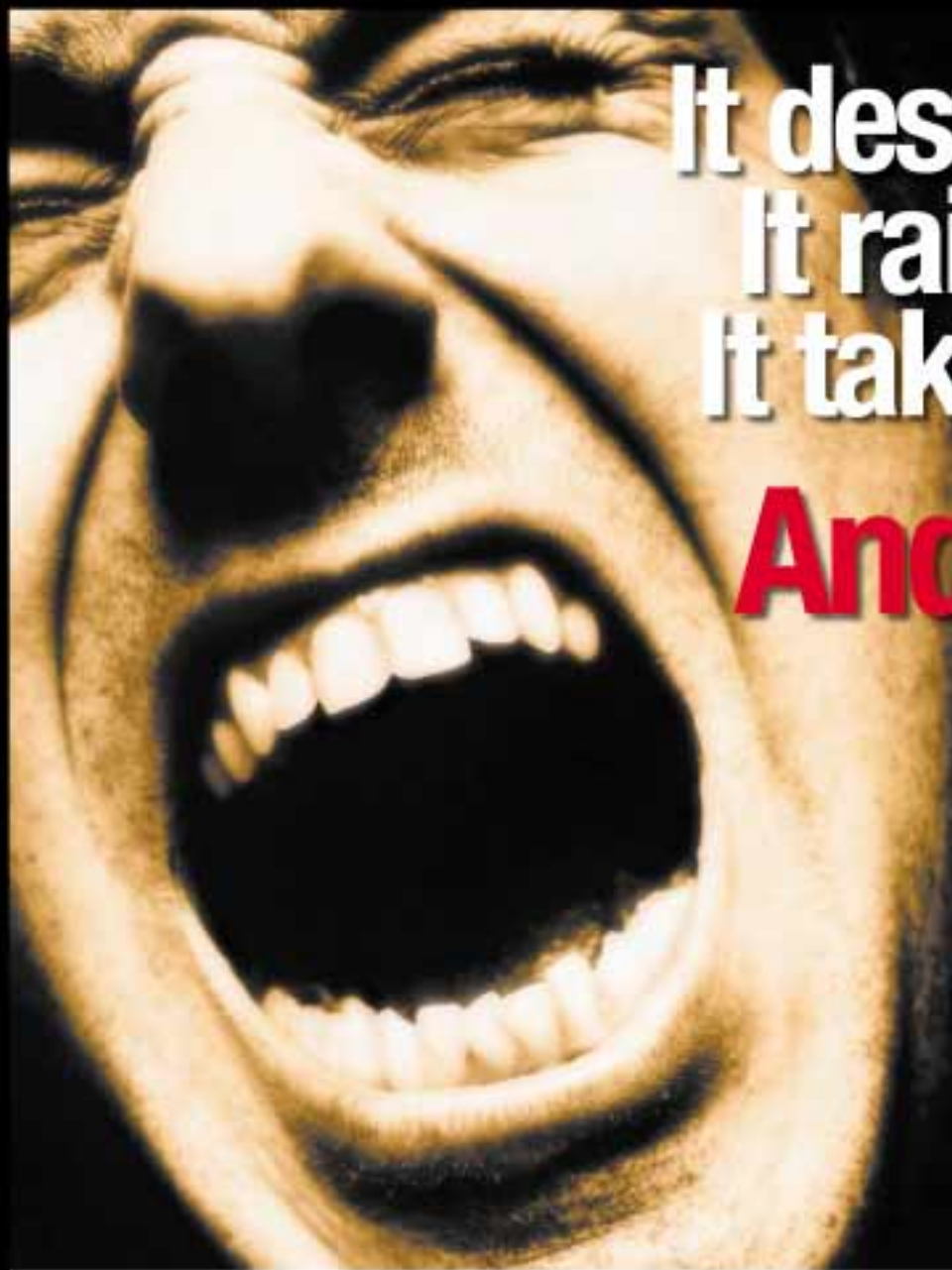
The current Congress is spending our present taxes and our future retirement funds, and creating a huge national debt on which we'll pay interest for years. The federal government is spending more per family than at any time in this century except for the three years of World War II when government commanded all of our national resources.

You bet, "It's the spending, stupid."

And if we don't remind politicians of both parties that they can't buy our votes with our own money, they'll keep on spending. They're digging a huge hole for us and our children.

You know the solution to that: When you're in a deep hole, stop digging! That's the Savage Truth.

Chicago Sun-Times columnist Terry Savage, a registered investment advisor, is on the board of the Chicago Mercantile Exchange. She can be reached at <http://www.terrysavage.com>. This article was first published by the Chicago Sun-Times on April 1, 2004. ©2004 Terry Savage Productions



**It destroys your jobs.
It raises your taxes.
It takes your money.
And it's all legal.**

**Best to Worst
Legal Systems**

Delaware	1
Nebraska	2
Virginia	3
Iowa	4
Idaho	5
Utah	6
New Hampshire	7
Minnesota	8
Kansas	9
Wisconsin	10
Indiana	11
Maine	12
Colorado	13
Arizona	14
Wyoming	15
North Dakota	16
South Dakota	17
Connecticut	18
North Carolina	19
Vermont	20
Maryland	21
New York	22
Michigan	23
Washington	24
Tennessee	25
New Jersey	26
Oregon	27
Massachusetts	28
Georgia	29
Pennsylvania	30
Oklahoma	31
Ohio	32
Alaska	33
Nevada	34
Kentucky	35
Rhode Island	36
New Mexico	37
Florida	38
Hawaii	39
South Carolina	40
Missouri	41
Arkansas	42
Montana	43
Illinois	44
Texas	45
California	46
Louisiana	47
Alabama	48
West Virginia	49
Mississippi	50

Your state's legal system may hurt you more than you know. Companies are hesitant to do business in a state with a reputation for unfair court systems. Lost business means lost jobs. Fewer workers bear a higher tax burden to pay for schools, roads and public services. Excessive lawsuits cost every American \$809* a year. It's enough to make you scream.

A recent Harris poll ranked the fairness of

all fifty states. If your state didn't make the top of the list, you are probably paying for it.

America needs legal reform now.

Demand that your elected officials fix the flaws in the justice system. Require fairness from your judges. For a copy of the survey and to learn how you can help, visit www.legalreformnow.com.

Lawsuit abuse hurts your state... and it hurts you.



www.legalreformnow.com



* A December 2003 Tillinghast Towers Perrin study estimated the cost of the U.S. tort system to be \$233 billion in 2002, or \$809 per U.S. citizen.

Paid for by the U.S. Chamber Institute for Legal Reform, 1615 H Street, NW, Washington, DC 20062-2000

Treasury Secretary Says Make Tax Cuts Permanent

by Daniel J. Mitchell

On March 25, U.S. Treasury Secretary John Snow hailed President George W. Bush's tax cuts in an article for *Newsday.com*.

"Thanks to the actions Congress took in passing the President's jobs-and-growth bill, the economy is now in strong recovery, with a GDP growth rate at 6.1 percent in the second half of 2003—the fastest six-month growth rate in nearly 20 years. Leading private forecasts are projecting growth of 4 percent plus for the 2004 year."

Snow continued, "In light of all this progress, it is extremely important to make the tax cuts permanent. The cuts have been the linchpin of the improving performance of the economy, and making those tax cuts permanent is the surest thing we can do to sustain the economy on a good, strong growth path for this year and for the years beyond."

Some critics of the Bush administration charge the tax cuts have dramatically reduced government revenues, causing big long-term deficits that will hurt the economy by driving up interest rates. That, however, is a misguided argument—not only because of a very weak relationship between deficits and interest rates, but also because historical budget data show tax revenues in future years will be at their historical average ... even if the Bush tax cuts are made permanent.

Snow judges even the current deficits "too large by far and unwelcome." But he also noted that "we [the administration] are going to do something about them." The President's budget calls for cutting the deficit in half over the course of the next five years, he added.

Tax Facts

During the 50 years from 1951 to 2000, federal tax revenues averaged 18.1 percent of gross domestic product (GDP). Opponents of tax relief frequently imply tax cuts have emptied government coffers and created long-term fiscal chaos, but tax revenues for 2012-2014 will average 18.1 percent of GDP, according to Congressional Budget Office (CBO) data. And that assumes the tax cuts are made permanent.

Critics correctly point out that tax revenues are currently below that level, but this is a short-term phenomenon resulting from the recent recession and the temporary stock market-driven collapse of tax revenues from capital gains. The CBO estimates tax revenues will soon be back at historical norms, averaging 18.1 percent of GDP over the 2007-2009 period.

That does not mean tax revenues should always be 18.1 percent of GDP. It is just a coincidence that average revenue collections and future revenue projections are

identical as a share of national economic output. It does, however, mean the Bush tax cuts will not cause future deficits.

Government Spending

Deficits, however, are not the issue. The real problem is government spending, and rising deficits are merely a symptom of that problem. This is true in the short run and the long run.

In the short run, federal spending has jumped dramatically, climbing from 18.4 percent of GDP in 2000 (the lowest burden of government since 1966) to more than 20 percent of GDP in 2004.

But that short-term expansion in the burden of the federal government is minor when compared to what will happen after the baby-boom generation begins to retire. Without reform, huge unfunded promises for Social Security and Medicare will cause an enormous increase in federal spending—and lawmakers just made the problem worse by creating a new entitlement for prescription drugs.

It is also worth noting that national defense expenditures are not the source of the problem. Defense spending today consumes only 4 percent of GDP. This is an increase compared to defense spending at the end of the Clinton administration, but it is very low compared to historical averages. For much of America's post-World War II period, defense spending averaged about 6 percent of GDP. Even during the Carter administration, when a weakened military capability led to serious international crises, national defense spending never fell below 4.7 percent of GDP.

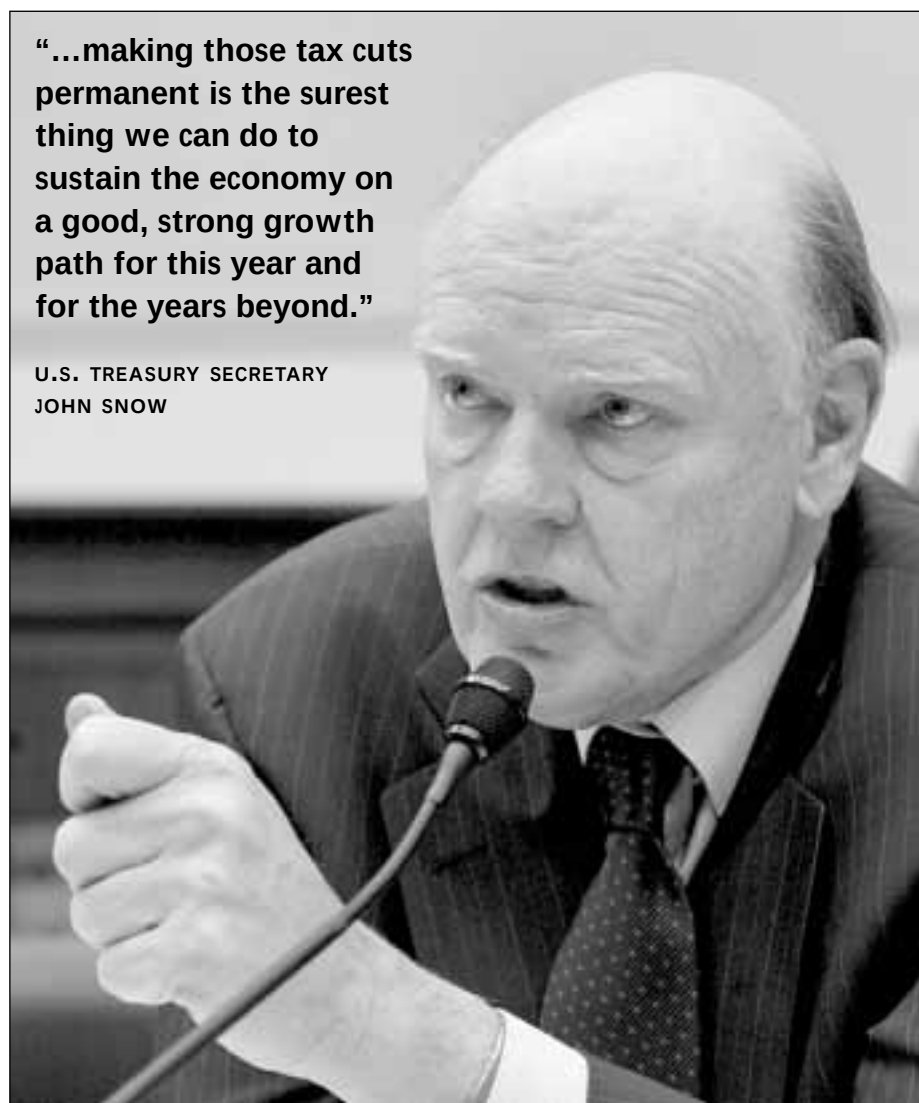
It is important to understand why government spending should be reduced (or at the very least, why its rate of growth should be slowed). Simply stated, the federal government squanders resources.

When politicians spend money, regardless of whether that spending is financed by taxes or borrowing, they are taking money from the productive sector of the economy and allocating that money on the basis of political rather than economic considerations. This inevitably weakens economic performance.

Government spending also undermines the nation's social fabric. When lawmakers increase government spending to address a problem previously handled by families, communities, and local governments (such as education, shelter, or health care for the indigent), people in local communities lose their initiative and incentive to address the needs of their neighbors. Moreover, the federal government generally does a poor job of addressing the problem since decision-making shifts to bureaucrats who frequently have no connection to the local problem.

"...making those tax cuts permanent is the surest thing we can do to sustain the economy on a good, strong growth path for this year and for the years beyond."

U.S. TREASURY SECRETARY
JOHN SNOW



Reuters Photo Archive

U.S. Treasury Secretary John Snow testifies before Congress on March 25.

In other words, when the federal government increases outlays for social programs, it causes social damage in a way that is similar to the way it harms overall economic performance.

Lower spending would be a good idea even if the federal government had a giant surplus. Regardless of whether the budget is in surplus or in deficit, government inevitably wastes money and deprives the private sector of resources that could be used to boost jobs and create growth.

That is why discretionary spending should be reduced, including a long-overdue re-examination of entire programs, agencies, and departments. Lawmakers should also reform entitlement programs, in part to reduce long-term budget pressures, but also because private-sector methods are better at providing health care and retirement income.

Deficit Debate a Charade

Today's deficit debate is largely a charade. Proponents of big government shed crocodile tears about the deficit because they

want higher taxes. Yet historical evidence clearly shows higher taxes would encourage additional spending and hurt the economy—and this would cause the deficit to climb even higher. Even more worrisome, this approach would hurt U.S. competitiveness, making America more like France and other European welfare states.

To save our children and grandchildren from that dismal fate, we need to keep cutting taxes and finally get serious about reducing the burden of government spending.

"Passing the President's budget for Fiscal Year 2005 means making the critically important tax cuts permanent. To do otherwise would mean that the American people face a significant tax increase. And that would be the wrong medicine," concluded Treasury Secretary Snow.

Daniel J. Mitchell, Ph.D., is McKenna Senior Research Fellow in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation. His email address is staff@heritage.org.

Federal Deregulation Could Cut Gas Prices

by Ben Lieberman

Everyone knows the recent rise in the price of oil has had an effect at the pump, but something less well known is also affecting gasoline prices. It is something the federal government could reduce, since the federal government created it in the first place. It is gasoline regulations.

Until the mid-1990s, the feds did not micro-manage the recipe for gasoline, the only exception being the phase-out of lead in the 1970s. But that changed with the 1990 amendments to the Clean Air Act, which began to take effect a few years later.

As a result of those provisions, we now have a bewildering variety of gasoline requirements. One-third of the nation uses reformulated gasoline, designed—very imperfectly, as it turned out—to address summer smog in the nation's most polluted metropolitan areas. We also have oxygenated gas in several areas to combat high wintertime levels

Gasoline in the more expensive cities (mostly in California) currently costs as much as 75 cents per gallon more than in the cheapest cities. Clearly there is more going on than an increase in the price of oil, which is the same everywhere. Not coincidentally, the most expensive cities also have the most onerous regulatory requirements.

Gas usually gets pricier heading into the summer months, as demand picks up and even tougher regulations designed to fight smog take effect. Given March's starting point of \$1.77, which is unusually high, this summer could prove to be very costly. Breaking the inflation-adjusted record of \$2.90 per gallon set in 1981 seems out of reach, but it's far from impossible.

Policy Implications

When gas price spikes occur, the policy debate never fails to focus on the high cost of crude—the regulatory burden generally gets ignored. True to form, Washington has yet to do anything sub-

“[I]f today's high prices persist well into the summer—especially the summer of an election year—we may see some serious efforts to tackle the federal red tape strangling the nation's gas pumps.”

of carbon monoxide, a problem that was rapidly disappearing even before the provisions took effect. In addition, conventional gasoline is also subjected to a number of requirements, which can vary by geographic location and time of year.

Several states also have come up with their own unique gasoline blend requirements, often in order to obtain required federal approval of their pollution-fighting plans.

Some of these measures have helped reduce vehicle emissions and improve air quality, while others have not. All, however, have succeeded in driving up the cost at the pump. In addition to the compliance costs of each regulation, the fact that we have gone from an efficient, national market in gasoline to a patchwork of regional, state, and local ones adds to the logistical costs for meeting the nation's fuel needs.

The impact of these regulations, some of which are still being phased in, has become especially noticeable in recent years. During periods when high oil prices boost gasoline prices, the total effect can be very punishing on working families.

stantial to reduce the regulatory burden, despite the specter of \$50 summertime fill-ups just months before the fall elections.

There is little the feds can do, at least in the short term, to address high crude oil prices. Opening up the Arctic National Wildlife Refuge and other U.S. sites to drilling would help, but would take several years. Tapping the 600 million barrels of oil in the Strategic Petroleum Reserve (SPR) is a short-term option, but the SPR was meant for national emergencies that disrupt oil supplies to the U.S. If used now simply to temporarily reduce today's high prices, the reserve would not be available later until it is replenished.

By contrast, streamlining the regulations could do some good, even in the short term, but doing so is politically difficult. The necessary changes to the Clean Air Act's gasoline requirements would spark loud environmentalist opposition.

If anything, policymakers may be heading in the wrong direction. The proposed energy bill, currently stalled in Congress, is at best a mixed bag on gaso-



A sign listing the prices for gasoline at a Union 76 gas station in Beverly Hills, California, April 20, 2004. Gasoline prices continue to rise in California due to special formulations of gasoline that are required to be sold in the state in an effort to combat air pollution.

line. It would modestly streamline a few of the fuel regulations, but also would add new ones, in particular a mandate that ethanol be added to gasoline.

According to the Department of Energy's Energy Information Administration, once fully implemented the energy bill may actually add up to three cents to the price per gallon.

Washington's relative indifference to the problem of high gas prices may not last long. While comparable gas price spikes occurred in 2000, 2001, and 2003,

none lasted more than two months. When prices fell, so did the public outcry for Congress to do something.

By contrast, if today's high prices persist well into the summer—especially the summer of an election year—we may see some serious efforts to tackle the federal red tape strangling the nation's gas pumps.

Ben Lieberman is a senior policy analyst at the Competitive Enterprise Institute. His email address is blieberman@cei.org.

Poll: 61% Support Abolishing Death Tax

by Ed Patru

A large majority of Americans believe the estate tax, also known as the "death tax," should be permanently repealed, according to a new survey released March 22 by the American International Automobile Dealers Association (AIADA).

The survey, conducted by McLaughlin & Associates in late February among 1,000 likely voters, found nearly two-thirds (61 percent) feel the estate tax should be abolished because it is inherently unfair.

"Voters across party, ideological, and demographic lines consider it to be unfair that the government taxes the earnings of individuals, and again taxes the estate at the time of the earner's death," noted pollster John McLaughlin, who shared the findings of the poll at an AIADA-sponsored congressional briefing on Capitol Hill. "Nowhere among the major voter groups do we see less than 70 percent of the voters saying it is unfair."

The poll found voters support permanent repeal by a 3:1 margin. According to the poll, 61.6 percent of respondents support permanent repeal; 18.7 percent oppose permanent repeal.

When asked whether it is fair or unfair to tax earnings when they are earned and again after the earner dies, 84 percent of survey respondents said they considered that to be unfair. Ninety-two percent of self-described "conservative" voters believe the death tax is unfair, as do 73 percent of self-described "liberals."

"Like many Americans, I believe the Death Tax is fundamentally unfair. It's a tax on assets I have created and paid taxes on," explained AIADA member Jeff Davis, an Ohio auto dealer who served as a panelist at the briefing AIADA called to unveil the survey results.

"I can tell you without reservation that if my businesses were forced to pay a 55 percent tax on our total net worth, we could not survive," Davis continued. "In all likelihood, my 11- and 12-year old children would lose the family business."

The poll also found:

- Most Republicans, Democrats, and Independents favor permanent repeal.

According to the survey, 73.2 percent of Republicans support permanent repeal, as do 50.3 percent of Democrats and 61.3 percent of Independents.

- Support for permanent repeal transcends ideological lines. Self-described conservative Republicans (77.7 percent) and moderate Republicans (69.6 percent) support permanent repeal. Among liberal Republicans, support for permanent repeal is at 59.5 percent. Even self-described conservative and moderate Democrats support permanent repeal, 60.9 percent and 51.4 percent, respectively. Only among self-described liberal Democrats is support for permanent repeal below 50 percent (44.5 percent).

- Income is irrelevant to voters' feeling that the death tax is unfair. Among voters earning less than \$40,000 per year, 84 percent feel the death tax is unfair; 12 percent feel it is fair. Among voters earning more than \$100,000, 82 percent view it as unfair, while 11 percent view it as fair.

- Most minorities support permanent repeal. According to the survey, 56.4 percent of African-Americans and 51.4 percent of Hispanics support permanent repeal of the tax. Among Caucasian voters, 63.5 percent favor permanent repeal.

- The majority of both men and women favor permanent repeal. Among men, 62.9 percent favor permanent repeal of the tax; among women, 60.0 support permanent repeal.

- Most Americans, regardless of age, support permanent repeal. Sixty-seven percent of likely voters age 41-65 support permanent repeal; among likely voters age 56-65, support for permanent repeal is at 63.6 percent. Likely voters over the age of 65 support permanent repeal at a rate of 61.9 percent. Among 26-40 year-olds, support for permanent repeal is at 53.2 percent. Only among likely voters age 18-25 is support below 50 percent (48.2 percent).

"The findings of this poll deal a serious blow to opponents of death tax repeal who argue the tax is fair. Voters recognize double taxation when they see it, and they don't like it—regardless of whether they

are personally affected by it," commented AIADA Chairman Buzz Rodland.

"As someone who owns and operates a small business, I feel confident in saying that our economy would see a significant increase in new job creation if small business owners were not saddled with the burdens of the Death Tax," added Davis. "In my case, there's no question that I waste countless hours and resources on estate planning.

"Last year," he continued, "I spent over \$35,000 on estate planning. This does not include the thousands spent on insurance for my wife and me. It does not include a \$40,000 business appraisal expense—something I wouldn't have had to do were there not a looming Death Tax."

"In today's competitive environment, automobile dealers need predictability in the tax code in order to buy new equipment, expand business opportunities, and create more jobs," points out AIADA board member Jenell Ross, a Dayton, Ohio auto dealer who seven years ago

nearly lost her business after the untimely death of her father. "My family's experience with the death tax has been eye-opening, and it has motivated us to do what we can to help bring an end to this unfair tax."

The survey of 1,000 randomly selected likely voters was conducted on February 23-24, 2004. All interviews were conducted via telephone by professional interviewers. The margin of error is +/- 3.1 percent.

Ed Patru is communications director for the American International Automobile Dealers Association. His email address is PatruE@aiada.org.

INTERNET INFO

For more information about the American International Automobile Dealers Association, visit its Web site at <http://www.aiada.org>.

TAXES



NFIB Praises Senator Nickles for Death Tax Repeal Effort

by John Skorburg

The National Federation of Independent Business (NFIB) on March 8 praised U.S. Senator Don Nickles (R-Oklahoma) for including in the Senate's 2005 budget a provision that would accelerate by one year complete repeal of the federal estate tax. Nickles' budget provides for elimination of the tax in 2009.

"Death-tax repeal is a big deal to NFIB's 600,000 Main-Street-owner members and this provision is one more shoe of dirt in the effort to bury it for good," said Jack Faris, president and

CEO of NFIB. "Eliminating the death tax in 2009 will give small-business owners two full years of freedom from this burdensome and unfair tax," Faris continued. "NFIB appreciates Sen. Nickles' continued efforts in this fight."

NFIB—with 600,000 members, the nation's largest small business advocacy group—is alerting senators it will consider any attempt to strike or water down the death tax repeal acceleration to be a "key vote" against its members' interests.

"This vote presents some senators and groups with the opportunity to do

some real mischief. NFIB wants to make sure it's clear: Giving small-business owners one more year of a more fair tax code is a step in the right direction to full repeal. Our goal continues to be the permanent repeal of a tax that unfairly levies a double tax on America's small-business owners, but in the meantime we certainly support this big step forward," Faris said.

Although the 2001 tax package repeals the death tax in 2010, it will rise from the dead—back to 2001 levels—the following year, unless Congress approves legislation making the

repeal permanent.

"People who want the death tax to come back from the dead just love to engage in a lot of class warfare," Faris concluded. "But the fact is that billionaires with names like Gates just set up tax-free foundations to shelter their money from this and other taxes. The people left holding the bag are the ones who get laid off when a small business is sold to deal with the death tax."

John Skorburg is managing editor of Budget & Tax News. His email address is skorburg@heartland.org.

Florida

Continued from page 1

trying to accomplish, saving money or improving service.”

The audit report went on to add that government employees negotiating the contracts “often lacked training or experience to pick the appropriate vendor or write the best contract.” Once the contract is in place, state agencies may have little authority to oversee services or determine if the state is getting its money’s worth. The report also revealed “there is no clearinghouse across state government that maintains records of vendor performance to insure that a bad vendor doesn’t win a second state contract while failing at the first.”

As Inspector General Derry Harper wrote, “As documented in almost 500 audit findings over a three-year period, controls over contracting [in Florida] are in a state of disrepair.”

Mission and Goals

In response, Bush has created the Governor’s Center on Efficient Government. Its mission is “to be the enterprise-wide gateway for best business practices in outsourcing in order to improve the way state agencies deliver services to Florida’s citizens.” In other words, to standardize how the state identifies and awards contracts for privatized government services.

The Center has three initial goals:

- Develop statewide outsourcing standards and a business case template applicable to any proposed outsourcing project;
- Review existing outsourcing plans within state agencies to ensure compliance with Center standards and business case, execution of effective contract language with vendors, and implementation of successful change management; and
- Propose for the Governor’s consideration by July 1, 2004 an initial list of specific outsourcing projects and initiatives that can be developed over the next three years.

“[The mission of] the Governor’s Center on Efficient Government [is] ... to standardize how the state identifies and awards contracts for privatized government services.”

Bill Simon, secretary of the Florida Department of Management Services, said “technological progress has also made the timing right for an outsourcing revolution.”

Initiatives Underway

Florida has been at the forefront of privatization for years. The past three administrations have supported several

initiatives, and Bush has been an ardent supporter of privatization and results-based government.

“If we can find a better way to send out payroll, handle purchasing, get licenses renewed online, provide medical services in public institutions ... and we can save money and add value to services, I will look at it,” Bush has said.

Dozens of privatization initiatives are currently underway in Florida, many started and completed under Bush and his team. Some of the current state privatization initiatives include:

- Aramark employees now serve food to state prisoners;
- Barton Protective Services employees collect fees on the state’s tollways;
- Health Management Systems Inc. administers Medicaid billing;
- Accenture workers staff the desk that state employees call to get help with their desktop computers; and,
- Private companies clean state buildings.

Despite the success of these initiatives, the administration has come under fire for failing to approach privatization strategically. Each initiative has been the “flavor of the day,” lacking a replicable decision-making matrix, standards, or procedures. No process has been developed for identifying future opportunities or conducting privatization studies.

Gary Van Landingham, interim director of the Legislature’s Office of Program Policy Analysis and Government Accountability, said, “It’s hard to tell how

things are working and whether privatization is achieving goals the policy makers were trying to reach. In some cases it’s been planned well and worked well and in some cases it hasn’t. There’s just a lack of common business analysis.”

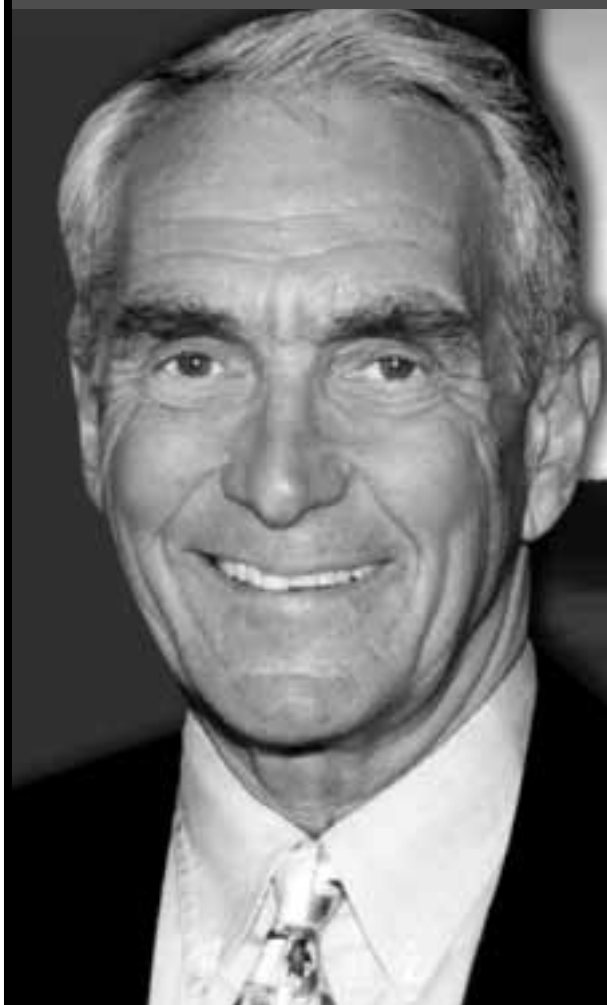
When asked in a recent interview to speculate on services that shouldn’t be privatized, the governor paused and answered, “corrections officers. ... I think police functions, in general, would be the first thing to be careful about outsourcing or privatizing. This office. Offices of elected officials ... and major decision-making jobs that set policy would never be privatized.”

Bush’s caution notwithstanding, Florida currently contracts with five private adult correctional facilities and numerous juvenile facilities.

The creation of the Center for Efficient Government signals a commitment to privatization in Florida. But more importantly, it also signals a serious commitment to providing the best services at the best cost for Florida taxpayers. The standards, processes, and framework that will be created over the next few months likely will serve as templates for other states to use. In fact, the Center itself should serve as a model for other states to follow.

Geoffrey F. Segal is the director of privatization and government reform policy at Reason Foundation. He is serving as an advisor to the Center for Efficient Government. His email address is geoffrey.segal@reason.org.

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Chicago Considers Privatizing Toll Road Linked to Indiana

by John Skorburg

The *Chicago Sun-Times* and other local media outlets reported on March 2 that the city-owned Chicago Skyway toll road may be sold to a private operator.

"Two years after raising the possibility of unloading the white elephant-turned-cash cow, Mayor Daley took the first concrete step toward privatizing it," noted the *Sun-Times'* city hall reporter, Fran Spielman.

Spielman reported city officials have issued a "request-for-qualifications" to private toll operators to gauge interest in the 7.8-mile roadway connecting Chicago and Northwest Indiana. Several dozen bids are expected.

"If those vying for the prize pledge enough cash, responsibility for operating and maintaining the Skyway could be turned over to a private operator by year's end," wrote Spielman. Annual operating and maintenance expenses for the Skyway currently run \$12 million, and \$400 million in debt remains.

Precedents Abound

The *Chicago Tribune's* transportation expert, Gary Washburn, noted, "Privately owned toll highways now operate in several countries, including Canada, Spain, and New Zealand." In 1999, a toll road serving metropolitan Toronto was sold for \$2.1 billion.

And that's not the only case, notes Robert Poole, director of transportation studies at the Reason Public Policy Institute. "Italy sold its major state-owned tollway agency in 1999 for \$6.7 billion; Portugal did likewise that same year; and Spain sold its one remaining state tollway last year for \$1.8 billion."

According to privatization expert Peter Samuel, editor and publisher of *Toll Roads Newsletter*, "Growing empirical evidence suggests that moving to private management and/or ownership is a superior arrangement. Such ... privatization can tap the expertise and other resources of private firms while at the same time avoiding the bureaucracy and perverse incentive structures that characterize the government sector."

In a 1996 report for The Heartland Institute, Samuel documented several toll road privatization successes in the U.S. and worldwide:

"In Virginia, the Dulles Greenway is a totally investor-built and -operated toll road. So are the 91-Express Lanes in the Los Angeles area. Smaller investor-built toll facilities have been built in Alabama and are under construction in Utah, Florida, and Texas, and others are being designed in Florida and California.

"Tollways in Orlando, southern California, and Colorado are still formally state or local government entities, but the overwhelming bulk of their operations is con-



Chicago Skyway

The Chicago Skyway is the only toll highway in Illinois that is not operated by the Illinois Toll Highway Authority. It is operated and maintained by the Streets and Sanitation Department of the City of Chicago.

Opened to traffic in 1958, the Chicago Skyway is a 7.8-mile toll bridge connecting the Dan Ryan Expressway (I-94) around Chicago to the Indiana Toll Road in Indiana; it is a shortcut between the City of Chicago and the State of Indiana. Automobiles currently pay a \$2 toll for one-way use. A McDonald's restaurant is available to motorists at the Skyway rest stop approximately at the road mid-point.

The Chicago Skyway does not carry any highway designation. Originally, it was designed as a portion of Interstate 90, but the City of Chicago discovered the

Chicago Skyway never received this official interstate designation. Thus, all the I-90 signs along the skyway have a "TO" sign placed over them instead of any official designation.

In 2002, before construction-related delays forced motorists to seek alternative routes, the Skyway attracted a record 18.7 million motorists and took in \$43 million in annual revenues—double the \$21.5 million in toll revenues in 1993. A \$250 million rebuilding of the road began in 2001 with main road work due to end in fall 2004.

According to the *Chicago Tribune*, in 2003, the Skyway served 17.4 million vehicles and generated \$39.7 million in toll revenues.

—Chicago Department of Transportation

tracted out, so only a small number are on government payroll. Few people probably know it, but the Detroit-Windsor tunnel is privately owned, as is the Ambassador bridge between Michigan and Canada.

"A similar trend toward privatization is taking place internationally. Toronto's 407-ETR, the world's most advanced automated toll road, is fully privatized, as is the world's second automated highway, Melbourne CityLink in Australia. The formerly government-owned Autostrade SPA, which operates most of Italy's motorways, is in the process of privatization. France's Cofiroute SA, which generates more revenue than any U.S. toll agency, is investor-owned."

Skyway Proposal

Why consider privatizing the Skyway? Chicago's recently appointed budget director, John Harris, explained simply, "The city gets to cash in the equity value in the Skyway and use it to pay off existing debt and finance core city services."

The Skyway's \$2 toll was last increased in 1993, and Harris told Spielman a new increase would be likely under a private contractor. "Over time," Harris noted, "tolls would have to meet the cost of operating and maintaining the facility as well as provide a reasonable return on the private operator's investment. But rates

would need to remain fair and reasonable in order to continue to attract users," he pointed out.

The agreement, Harris added, would be for a term of no less than 50 years, "to give the buyer adequate title to claim depreciation" under federal tax rules. The private contractor would be expected to "bring to bear experience and expertise in operating toll-ways around the world in a very cost effective and efficient manner."

Correct Road to Travel?

"There is everything to gain and little to lose by calling for competitive proposals from investors ... on how they would operate and improve these facilities for the public, and on what terms," noted Peter Samuel. "With a set of real proposals on the table, open to full public scrutiny, there will be a chance for a more businesslike system to evolve, to the benefit of everyone who uses (or relies on others who use) the region's highways."

According to Spielman, "With less 'skimming' and reduced labor costs, transportation experts said a private operator could provide improvements like better snow removal. But they warned that City Hall had better be prepared to spell out expectations in 'excruciating detail' and make certain those standards are met."

"If they're not prepared to do that,

there's going to be a problem. You can look at Hired Trucks [scandal] as a classic example of what happens when there isn't adequate follow-through," said Dave Schulz, the former city budget director who now runs Northwestern University's Infrastructure Technology Institute.

Reason's Poole agrees: "Obviously this needs to be done carefully. But with ample precedents to draw from, Chicago should be able to pull this off successfully, to the great benefit of Chicago taxpayers."

John Skorburg is managing editor of Budget & Tax News. His email address is skorburg@heartland.org.

INTERNET INFO

Peter Samuel's December 1999 *Heartland Policy Study*, "The Illinois Tollway: An Opportunity for Reform," is available on The Heartland Institute's Web site at <http://www.heartland.org/Article.cfm?artId=9436>.

For a wealth of information on tollway privatization and more, visit the Web site of the Reason Public Policy Institute at <http://www.rppi.org>.

Reps Warn Foreign Capital Will Leave if IRS Regulation Is Not Withdrawn

by **Veronique de Rugy**

Led by Rep. Mark Green (R-Wisconsin), a member of the House Banking and Financial Services Committee, 28 members of the U.S. House of Representatives wrote Treasury Secretary John Snow on March 18, urging him to "quickly withdraw" the Internal Revenue Service's proposed interest reporting regulation. The lawmakers warn the initiative "would have a very harmful effect on our economy and cause much-needed capital to leave the United States."

"These 28 Members of Congress understand that it would be a mistake to drive capital out of the U.S. economy."

ANDREW QUINLAN

The regulation, first proposed during the final days of the Clinton administration and then cosmetically modified in 2002, would require banks to report interest paid to nonresident aliens—even though this information is not needed to enforce U.S. law. The IRS initiative has generated considerable opposition from critics who fear many foreigners would withdraw their money from U.S. banks, harming the economy and undermining the global competitiveness of U.S. financial institutions.

The federal lawmakers' outreach to Snow was applauded by many.

"The Center for Freedom and Prosperity and the Coalition for Tax Competition applaud the leadership of Rep. Mark Green and congratulate the members of Congress who have joined with him in fighting for America's economy," said Andrew Quinlan, president of the Center for Freedom and Prosperity. "These 28 Members of Congress understand that it would be a mistake to drive capital out of the U.S. economy."

Dan Mitchell, tax expert for The Heritage Foundation, agreed, noting, "The IRS interest-reporting regulation was a bad idea when first proposed during the final days of the Clinton administration and it is a bad idea today. It is anti-tax reform, anti-competitive, and it will hurt the U.S. economy. Secretary Snow should uphold the law and require that the ideologically motivated bureaucrats at the IRS withdraw this misguided proposal."

One hundred lawmakers—18 Senators and 82 Congressmen from 39 states—two federal agencies, every major financial industry association, and 40 public policy organizations have denounced the proposed regulation.

Veronique de Rugy is a fiscal policy analyst for the Cato Institute. Her email address is vderugy@cato.org.

INTERNET INFO

For more information visit the Web site of the Center for Freedom and Prosperity at <http://www.freedomandprosperity.org>.

LETTER

March 18, 2004

The Honorable John Snow
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, D.C. 20220

Dear Secretary Snow:

We are writing to express our strong objection to the Internal Revenue Service's (IRS) Regulation (REG-133254-02) that, if implemented, would have a very harmful effect on our economy and cause much-needed capital to leave the United States. The latest version of this proposed rule would compel U.S. banks to report the deposit interest they pay to selected non-resident aliens. This is bad economic policy, bad regulatory policy, and bad tax policy. Originally proposed by the Clinton administration, this policy does nothing to aid in job creation or economic growth, and is a direct threat to America's long-term economic interests.

Congress decided long ago that taxing foreign-owned capital deposited in U.S. banks was bad policy. Instead, lawmakers allowed foreigners to bring their money here, tax-free. As a result, American financial institutions have about \$2.3 trillion in foreign funds. These funds work their way through the economy as loans for cars, homes, and business expansion, eventually creating jobs and enhancing economic growth.

This new rule fortunately would apply only to a portion of this capital, but it nonetheless is bad economic policy since it will discourage and more than likely reverse the flow of capital to America. Indeed, more than \$40 billion on an annualized basis was withdrawn from foreign-owned U.S. savings accounts in the first quarter of 2001, in large part because the regulation was first announced on January 17 of that year. We don't know how much capital will leave if the regulation is implemented. Suffice to say that any loss of funds is going to hurt our capital markets and make it harder for consumers and businesses to access credit. The regulation also will undermine the safety and soundness of our banking sector, a point that already has been raised by the Chairman of the Federal Deposit Insurance Corporation.

The IRS initiative also is bad regulatory policy. For more than 80 years, Congress has made a deliberate effort to create policy and approve laws to attract capital to the U.S. economy. It is rather disturbing, therefore, to see the IRS attempt to overturn the democratic process with bureaucratic edict.

Last but not least, the regulation is bad tax policy. As you well know, the president is trying to slowly but surely reform our tax code by eliminating different forms of double-taxation. The IRS is undermining this effort by seeking to help foreign governments double-tax the interest paid to non-resident aliens who have invested in the U.S. economy.

We hope you will quickly withdraw this misguided regulation. The IRS should not be allowed to overturn the law, especially when the result will hurt America's economy.

Sincerely,

Mark Green	Butch Otter	Roger Wicker	Phil Crane
Roscoe Bartlett	Gary Miller	Jim DeMint	Nathan Deal
John Sullivan	Tom Reynolds	Mark Foley	John Culberson
Mark Kennedy	Walter Jones	Pat Toomey	J. Gresham Barrett
Ron Paul	Joe Pitts	John Shadegg	Sue Myrick
Lee Terry	Todd Akin	Pete Sessions	David Vitter
Jeff Miller	Scott Garrett	Chris Cannon	Chris Chocola

cc: Vice President Richard Cheney
CEA Chairman Greg Mankiw
NEC Chairman Steve Friedman



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Trade War with EU Heats Up

Texas taxes and agriculture tariffs caught in crossfire

Oby John Skorburg
 n March 1, the European Union imposed an estimated \$300 million in trade sanctions against the United States for Congress's failure to repeal the Foreign Sales Corporation (FSC) legislation first deemed illegal by the World Trade Organization two years ago. (See "US and EU on Collision Course over Taxes," *Budget & Tax News*, December 2003.)

According to the Web site of the United States Mission to the European Union, "The United States lost successive [FSC] cases in the WTO, which determined that the tax breaks in those laws amounted to export subsidies in violation of WTO rules. The WTO ruled that the EU—which brought the formal complaints—is entitled to impose more than \$4 billion in retaliatory trade sanctions. The EU began imposing 5 percent retaliatory tariffs on some U.S. products on Mar. 1 and said it would phase in higher tariffs unless the export break is repealed."

"The name of the game is repeal. It is not retaliation, not sanctions. It is repeal, and to have a WTO-compliant legislation," said EU Trade Commissioner Pascal Lamy while visiting Washington DC in late February to discuss FSC reform legislation pending in Congress.

But by March 1, Lamy's mind had changed. "We are therefore left with no choices but to impose countermeasures," he said from Brussels.

The EU has never before imposed trade sanctions on U.S. exports under the WTO, and it appears eager to drop them once Congress has acted to clear up the matter. Both houses of Congress have before them measures that would bring the U.S. export tax program, the Extraterritorial Income Exclusion, into conformity with the nation's WTO obligations.

"The faster that they [Congress] get on [legislation], the faster we can lift the sanctions," Lamy's spokeswoman, Arancha Gonzalez, told AP correspondent Raf Casert in Brussels.

"We've urged the European Commission to refrain from imposing retaliatory tariffs, given the complexity of the [pending] legislation, and we regret that they are moving forward," said a spokesman for the U.S. Mission in Brussels. "But we will continue to work with Congress to get the legislation moving as quickly as possible."

Farmers Respond

With U.S. farmers facing higher tariffs

on sales to Europe, the American Farm Bureau Federation (AFBF) is urging Congress to bring U.S. laws into compliance with World Trade Organization rules as quickly as possible.

"Because of the higher tariffs the EU is imposing on raw agricultural products and the products processed from them, U.S. farmers have unfortunately been drawn into the WTO dispute and will suffer unless a solution to the problem is quickly found," said AFBF President Bob Stallman. "We urge Congress to act quickly to eliminate the threat of severe disruption that is certain to occur for U.S. exports."

"The EU sanctions could result in heavy losses to U.S. farmers and ranchers if Congress doesn't act soon," continued Stallman. "Not only is the U.S. agriculture industry facing higher tariffs on soybean meal and other commodities that only apply to U.S. products, we are competing with products from other countries with lower tariffs."

Tax Reform Good for Texas

Passage of the FSC reform measure could be good not only for agriculture, but also for states in the U.S. that do not have an income tax, according to reports in the *Paris [Texas] News*. A March 14 article notes, "Texans could receive a federal income tax deduction on sales tax payments if a measure considered in Congress becomes a part of a Foreign Sales Corporation bill."

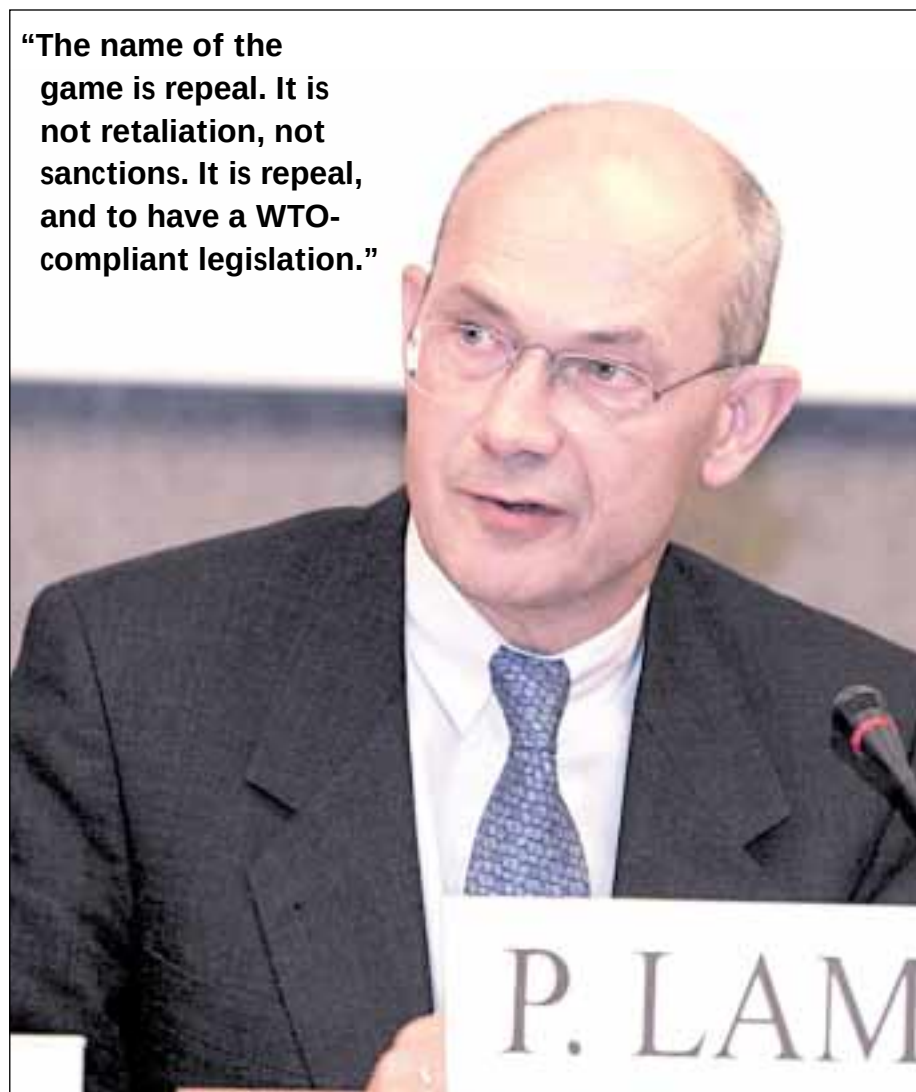
U.S. Rep. Max Sandlin (D-Texas) said on March 12 that a sales tax deduction "will be included in the Democratic version of the tax bill." Sandlin sits on the Ways and Means Committee, which has jurisdiction over all tax legislation, including the FSC reform measure. "I

"The EU has never before imposed trade sanctions on U.S. exports under the WTO, and it appears eager to drop them once Congress has acted to clear up the matter."

am gratified that we have this opportunity to promote fairness in our tax code," Sandlin said.

Seven states, including Texas, have no income tax. Taxpayers in those states are treated unfairly by the federal government, Sandlin said, because they have no state income tax payments that can be deducted from federal income taxes. "A sales tax deduction will level the playing field for residents of Texas, Florida, South Dakota, Tennessee,

"The name of the game is repeal. It is not retaliation, not sanctions. It is repeal, and to have a WTO-compliant legislation."



Though he noted in late February the European Union did not want to impose trade sanctions against the U.S., by March 1 EU Trade Commissioner Pascal Lamy said "we are left with no choices" but to do so.

Nevada, Washington state, and Wyoming," Sandlin said. "Texans will

the *Paris News* on March 13 that he supports the effort to allow Texans to deduct sales taxes. "We've been trying to get that done for the past 10 years," Hall said. But the congressman said he is opposed to bowing down to foreign nations who continue to make demands concerning trade. "I'm against anything the European Union does," Hall said. "We have given them way too much power."

The sales tax deduction and FSC reform measures are included in a bill pending in the Senate and a legislative proposal in the House of Representatives. Both would make far-reaching changes to the international corporate tax system. Action on the measures was expected before Congress adjourns for its Memorial Day recess.

John Skorburg is managing editor of *Budget & Tax News*. His email address is skorburg@heartland.org.

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